No. 7488.

7

In the United States Circuit Court of Appeals

For the Ninth Circuit.

Galen H. Welch, Collector of Internal Revenue for the Sixth Collection District of California,

Appellant,

vs.

The St. Helens Petroleum Company, Ltd., a corporation,

Appellee.

BRIEF FOR THE APPELLEE.

JOSEPH D. PEELER,
819 Title Insurance Bldg.,
Los Angeles, Calif.
Counsel for Appellee.

GEORGE M. WOLCOTT,
DONALD V. HUNTER,
922 Southern Bldg.,
Washington, D. C.
Of Counsel.

FILED
MAR 11 19[illegible]

Parker, Stone & Baird Co., Law Printers, Los Angeles.

TOPICAL INDEX.

PAGE

Opinion Below ... 3

Jurisdiction ... 3

Questions Presented ... 4

Statutes Involved ... 5

Statement of Facts ... 6

Preliminary Statement ... 8

Summary of Argument ... 10

Argument ... 13

Point I. The court below did not err in denying appellant's motion in arrest of judgment ... 13

(a) The Commissioner may not oust the court of jurisdiction by failing to advise the court whether or not new profits tax rates are required because of the court's correction of errors made by the Commissioner in determining appellee's net income ... 16

(b) The precedents cited by appellant do not support his contention ... 21

(c) The question of jurisdiction would in any event apply only to the profits taxes and not to the income tax ... 28

(d) The statute as construed by appellant would be of doubtful constitutionality ... 31

Point II. The court below did not err in holding that appellee was entitled to the deduction of income taxes paid by it to Great Britain ... 34

(a) Under our revenue acts the deduction for taxes is allowable to the one on whom the taxes were imposed and by whom they were paid ... 35

PAGE

(b) Under the British law the tax here in question was imposed on and was paid by the appellee 40

(c) Rule 20 of the British act does not operate to cancel any part of the income tax imposed on a British company, or to shift any part of that tax to the company's stockholders 41

(d) The deduction of a tax from dividends under Rule 20 of the British act does not in any real sense reimburse the company for its own income tax payment 58

(e) Appellant's construction of the law would result in administrative confusion and serious danger of duplicating deductions 64

(f) There has been no implied ratification by Congress of the interpretation for which appellant contends 66

Conclusion 69

INDEX TO APPENDIX.

Statutes 71

United States:

Revenue Act of 1921, Section 234 71

Revenue Act of 1921, Section 234 (b) 72

Revenue Act of 1921, Section 237 73

Revenue Act of 1921, Section 238 (a) 72

Revenue Act of 1921, Section 328 74

Great Britain:

Act of 1918, Section 23, Paragraph 444 78

Act of 1918, Section 237 77

General Rules Applicable to Schedules A, B, C, D and E, Paragraph 420 77

Schedule D, Paragraph 359 76

The Income Tax Act 1918 and Finance Acts 1919 to 1925 .. 76

TABLE OF AUTHORITIES CITED.

Cases. PAGE

American Chain Company v. Eaton, 291 U. S. 386 18
Appeal of R. C. Musser, 3 B. T. A. 498 36

Bailey v. George, 259 U. S. 16 17
Bankers Pocahontas Coal Company v. Burnet, 287 U. S. 308 15
Basil Robilland, 20 B. T. A. 685 67
Bernheim Distilling Company v. Mayes, 268 Fed. 629 18
Blair v. Oesterlein Machine Company, 275 U. S. 220 16
Bradbury (Collector of Taxes) v. English Sewing Cotton Company, Ltd., 8 British Tax Cases 481 46
Brown's "Shamrock" Linens, Ltd. v. Bowers, 48 F. (2d) 103 23

Central Iron and Steel Company v. United States, 6 F. Supp. 115 26
Cheatham v. United States, 92 U. S. 85 17
Chicago Frog & Switch Company v. United States, 67 Ct. Cl. 662 25
Child Labor Tax Case, 259 U. S. 20 33
Cleveland Automobile Company v. United States, 70 F. (2d) 365 25
Commissioner v. Rail Joint Co., 61 F. (2d) 751 39
Commissioner v. Van Dorst, 59 F. (2d) 677 18
Commissioners of Inland Revenue v. Dalgety & Co., Ltd., 15 T. C. 216 61
Cramer and King Company v. Commissioner, 41 F. (2d) 24 25

Darcy v. Commissioner, 66 F. (2d) 581 19
Duffin v. Lucas, 55 F. (2d) 786 18
Duquesne Steel Foundry Company v. Commissioner, 41 F. (2d) 995 25

Eisner v. Macomber, 252 U. S. 189 33

Factors and Finance Company v. United States, 73 Ct. Cl. 707, 56 F. (2d) 902 27
Field v. Clark, 143 U. S. 649 32
Freeport Texas Company v. United States, 58 F. (2d) 473 28

PAGE

George W. Elkins, Docket No. 75742 67

Graham v. Dupont, 262 U. S. 234 17

Hamilton v. Commissioner, 6 B. T. A. 240 36

Hamilton v. Commissioner of Inland Revenue, 16 British Tax Cases 213 42

Heiner v. Diamond Alkali Company, 288 U. S. 501 .... 22, 25, 26, 29, 30, 32

Heiner v. Diamond Alkali Co., 288 U. S. 502 20

Helvering v. Taylor, January 7, 1935 18

Helvering v. New York Trust Co., 292 U. S. 455 68

Hill v. Wallace, 259 U. S. 44 33

Hoeper v. Tax Commissioners, 284 U. S. 206 33

Howbert v. Norris, 72 F. (2d) 753 18

Inland Revenue Commissioners v. Blott, 2 A. C. 171 57

James Hickey, Estate of, Docket No. 75852 67

Jones v. Commissioner, 38 F. (2d) 550 18

Joseph Joseph & Bros. Company v. United States, 71 F. (2d) 389 25

Kilbourne v. Thompson, 103 U. S. 168 32

Klein v. Board of Tax Supervisors, 282 U. S. 19 33

Leslie H. Reed, Docket No. 75812 67

Liverpool and Great Western Steam Company v. Phoenix Insurance Company, 129 U. S. 397 5

Marie Cook Hickey, Estate of, Docket No. 75849 67

Mary Duke Biddle, Docket No. 62025 67

McDonnell v. United States, 59 Fed. (2d) 290 28

Monangahela Navigation Co. v. United States, 148 U. S. 312 32

Murray's Lessee v. Hoboken Land and Improvement Co., 59 U. S. 272 32

PAGE

Neumann v. Commissioners of Inland Revenue, 150 Law Times Reports 481, 18 British Tax Cases 332 ..... 45, 49

New York Life Insurance Company v. Anderson, 263 Fed. 527 18

Nichols v. Coolidge, 274 U. S. 531 33

Oak Worsted Mills v. United States, 38 F. (2d) 699 27

Omego Chemical Co., 31 B. T. A. No. 200 69

Panama Refining Co. v. Hopkins, 79 L. Ed. 223 32

Peterson v. Commissioner, 31 B. T. A. 172 36

Phillips v. Commissioner, 283 U. S. 589 32

Purdie v. Rex, 3 K. C. B. 112, 111 Law Times Reports 531 ..... 44, 55, 59

Railroad Supply Company v. Burnet, 51 F. (2d) 437 25

Ritson v. Phillips, 131 L. T. 384, 9 Tax Cas. 10 44

Sage v. United States, 250 U. S. 33 17

Schlesinger v. Wisconsin, 270 U. S. 230 32

Shearer v. Commissioner, 48 F. (2d) 552 35

Small v. Commissioner, 27 B. T. A. 1219 36

Snyder v. Marks, 109 U. S. 189 17

Strattons Independence v. Howbert, 231 U. S. 399 33

Tait v. Western Maryland R. Company, 289 U. S. 621 15

U. S. Paper Exports Ass'n v. Bowers, 6 F. Supp. 735 28

United States v. Carver, 260 U. S. 482 24

United States v. Cohen Grocery Co., 255 U. S. 81 32

United States v. Emeny etc. Co., 237 U. S. 28 17

United States v. Factors and Finance Company, 288 U. S. 89 ..... 20, 27

United States v. Hartwell, 6 Wall. 385 69

United States v. Henry Prentiss & Company, 288 U. S. 73 28

United States v. Merriam, 263 U. S. 179 32

PAGE

United States v. Rindskopf, 105 U. S. 418 ... 18

United States v. Supplee-Biddle Hardward Co., 265 U. S. 189 ... 26

W. H. Bradford and Company v. United States, 6 F. Supp. 117 26

Wickwire v. Reinecke, 275 U. S. 101 ... 18

Williamsport Wire Rope Company v. United States, 277 U. S. 551 ... 19, 22, 25

Wilson v. Eisner, 282 Fed. 38 ... 18

Yick Wo v. Hopkins, 118 U. S. 356-374 ... 32

STATUTES.

PAGE

British Income Tax Act of 1918, Section 237 ... 40

British Income Tax Act, Rule 1 of General Rules, Schedules A, B, C, D, and E ... 40

British Revenue Act of 1842, Section 1842 ... 43, 45

Finance Act, 1927 ... 5

Finance Act, 1930 ... 5

Finance Act of 1920, Section 27 ... 61

Finance Act of 1931, Section 7 ... 55

Judicial Code, Section 128 (a) ... 4

Revenue Act of 1917, Section 210 ... 27

Revenue Acts of 1918 and 1921 ... 11

Revenue Acts of 1918, 1921, 1924 and 1926, Sec. 234 (a) (3) ... 34, 35

Revenue Act of 1918, Sections 327 (b) and 328 ... 7, 13, 22, 23, 28

Revenue Act of 1918, Section 902 ... 37

Revenue Acts of 1918 and 1921, Section 233 (b) ... 39

Revenues Acts of 1918 and 1921, Section 234 (a) (3) ... 62

Revenue Act of 1921, Sections 327 and 328 ... 10, 14, 16, 21, 27, 29

PAGE

Revenue Act of 1921, Sections 327 (b) and 328....7, 13, 22, 23, 28
Revenue Act of 1921, Section 327 (d).......... 22
Revenue Act of 1921, Sections 232-236.......... 14
Revenue Act of 1921, Sections 234 (a) (7) and (9).......... 13
Revenue Acts of 1928, 1932 and 1934.......... 34
Revenue Act of 1932, Section 617.......... 37

United States Constitution, Article I, Section 1.......... 32
United States Constitution, Art. I, Section 8..........31, 32
United States Constitution, Art. III, Section 1.......... 32

TEXT BOOKS AND ENCYCLOPEDIAS.

Snelling's Dictionary of Income Tax and Surtax Practise.......... 5

MISCELLANEOUS.

A. R. R. 1020, C. B. I-2, p. 104.......... 37
A. R. R. 3041, C. B. II, p. 1100.......... 37

G. C. M. 630, C. B. IX-2, 107.......... 65
G. C. M. 7630, C. B. IX-2, 107.......... 38

Mem. 3988, C. B. XI-2, 25.......... 37

S. M. 3040, C. B. IV-1, 198.......... 64
S. M. 5363, C. B. V-1, 89.......... 64

No. 7488.

In the United States Circuit Court of Appeals

For the Ninth Circuit.

Galen H. Welch, Collector of Internal Revenue for the Sixth Collection District of California,

Appellant,

vs.

The St. Helens Petroleum Company, Ltd., a corporation,

Appellee.

BRIEF FOR THE APPELLEE.

OPINION BELOW.

The opinion of the court below, the District Court of the United States for the Southern District of California, which is unreported, is set forth on pages 37-39 of the Transcript of Record.

JURISDICTION.

This appeal involves income and profits taxes for the fiscal year ended May 31, 1921, and is taken from a judgment of the District Court entered in favor of the tax-

payer on November 17, 1933. [R. 24-25, 76.] The appeal is brought to this Court by petition for appeal filed by appellant on February 16, 1934 [R. 84], pursuant to Section 128(a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED.

1. The Commissioner of Internal Revenue was required to determine, and did determine profits tax rates of appellee, as a foreign corporation, by comparison with the rates paid by representative domestic corporations. Appellant concedes, and the trial court has found, that the Commissioner erroneously overstated appellee's taxable net income because of the disallowance of certain deductions to which it was entitled. The trial court redetermined appellee's profits taxes by applying to the corrected taxable net income the rates previously determined by Commissioner and redetermined the income tax by applying to the corrected net income the rate fixed by law. Was the Court without jurisdiction to change the amount of either the profits taxes or the income tax as determined by the Commissioner?

2. During the taxable year ended May 31, 1921, the appellee paid to Great Britain certain income taxes upon its profits and subsequently deducted a corresponding amount from dividends paid by it to its stockholders during said year. Were such taxes deductible from its gross income for said taxable year? The fundamental question is whether said taxes were imposed by Great Britain upon the corporation's income or upon the dividends paid to its stockholders.

STATUTES INVOLVED.

In an Appendix attached hereto are set forth the relevant provisions of the United States Revenue Acts, and also such provisions of the British statutes as were cited or quoted in the briefs below. At the hearing below the parties and the Court agreed that the Court might take judicial notice of the British law incorporated in the briefs of counsel. [R. 34-36.] In his brief herein, appellant has cited and quoted many additional provisions from the British statutes which were not cited in the briefs below. We respectfully submit such additional provisions are not in evidence and cannot be considered by this Court. (*Liverpool and Great Western Steam Company v. Phenix Insurance Company,* 129 U. S. 397, 446.) Included among the additional citations in the present brief of appellant are quotations from the *Finance Act, 1930* (Brief for Appellant, p. 37), and from the *Finance Act, 1927* [Brief for Appellant, Appendix B, p. 11] which obviously can have no bearing on the earlier years, here in question.

A similar question might be raised as to British judicial decisions which were not cited in the briefs before the Court below, but appellant is willing to assume, subject to the approval of this Court, that additional British decisions may be considered for the purpose of explaining the statutory provisions which are properly in evidence.

In any event, it seems difficult to reconcile with the stipulation below [R. 34-36], the copious quotations in appellant's brief (pp. 41-42, 44-45) from *Snelling's Dictionary of Income Tax and Surtax Practise,* apparently a recent text-book or treatise, not cited in any of the briefs below. [R. 34-36.] It is practically impossible to determine whether the author's comments, obviously directed

to current law, would apply equally to the British law in effect during the earlier years here in question.

For the above reasons, appellee is not attempting herein to cover any statutory provisions or text-book quotations which were not introduced into evidence below through citation in the briefs there submitted.

STATEMENT OF FACTS.

All the facts were stipulated. [R. 29-36, 41-64.] The appellee is a corporation organized under the laws of Great Britain having its principal office and place of business in Los Angeles, California. [R. 29.] During the fiscal year ended May 31, 1921, it accrued and paid to the Government of Great Britain an income tax in an amount, converted into United States currency, of $41,657.19. [R. 31.] During the same fiscal year its income from sources within the United States was 99.75 per cent of its total net income from all sources. [R. 31.] Appellee deducted from the dividends paid by it to its stockholders during said fiscal year an amount of at least $41,553.05, on account of said British taxes. [R. 31.] The parties hereto stipulated and agreed that if the plaintiff is entitled to a deduction, in determining its taxable net income, of income taxes so accrued and paid to Great Britain, the amount of said deduction for the fiscal year ended May 31, 1921, is $41,553.05. [R. 31.] The Commissioner of Internal Revenue allowed no deduction on account of said British income taxes for the fiscal year ended May 31, 1921. [R. 32.]

In its tax returns for the fiscal year ended May 31, 1921, appellee reported total taxes in the amount of $418,-292.95, which was duly assessed and paid to the then

Collector of Internal Revenue. [R. 30.] Upon an audit of the returns, the Commissioner of Internal Revenue determined a deficiency in tax for said year of $275,-202.52. [R. 44.] In determining said deficiency, the Commissioner redetermined appellee's profits tax liability for said fiscal year under the provisions of Section 328, Revenue Acts of 1918 and 1921. [R. 45, 60.] Said deficiency was duly assessed and paid by appellee to appellant as Collector of Internal Revenue on January 22 and March 11, 1929. [R. 30.]

Within the period and in the manner provided by law, appellee filed with the Commissioner of Internal Revenue a claim for refund, setting forth therein the same grounds alleged in its Complaint in the present proceeding. [R. 6-10, 13, 30, 74.] The Commissioner of Internal Revenue failed to take any action with respect to said claim for refund and after a lapse of more than six months, appellee filed its complaint in the present proceeding. [R. 11, 14-15, 74.]

By stipulation a jury was waived and the case was tried by the Court without the intervention of a jury. [R. 28, 72.] The parties filed with the Court a stipulation of facts, in which appellant stipulated that appellee was entitled to a further deduction for oil depletion in the amount of $12,000.00, and a further deduction for depreciation on wells in the amount of $6,604.41, for the fiscal year ended May 31, 1921. [R. 31, 74.] The parties left for determination by the Court the question of deductibility of the British income taxes. [R. 31.] At the close of all the evidence, counsel for each party moved for judgment on the record. [R. 36.] On September 21, 1933, the Court, by minute order ordered judgment in favor of appellee. [R. 37-39.] Pursuant to order of the Court

on motion to reopen the case for additional evidence, a stipulation of additional facts was filed on November 6, 1933. [R. 39-64.] Thereafter on November 10, 1933, appellant filed a motion in arrest of judgment, which was denied by the Court. [R. 65-68.] Appellant filed requests for special findings of fact and conclusions of law, which were rejected by the Court. [R. 68-71, 77.] The Court accepted and adopted the findings and conclusions of law requested by appellee. [R. 71-77.] The Court determined that the Commissioner had erred in refusing to allow to appellee deductions from income for the fiscal year ended May 31, 1921, in the amount of $12,000 for further depletion; in the amount of $6,604.41 for further depletion on wells; and in the amount of $41,553.05 for British income taxes, and in levying tax assessments on the basis of net income computed without the allowance of said deductions. [R. 76.] On this basis, the Court rendered judgment for the appellee for $25,782.58, with interest as provided by law. [R. 24-25.] From this judgment for appellee, the appellant has appealed. [R. 84.]

PRELIMINARY STATEMENT.

At the trial below, six associated cases were consolidated for trial, all being suits against present or former collectors of internal revenue for income or income and profits taxes alleged to have been erroneously collected. In each of these cases, judgment was entered by the Court in favor of the taxpayer, and all, upon appeal, have been set for argument together before this Court. Following is a list of these cases, showing the Docket No. in this Court, the names of the parties, and the fiscal year involved.

Docket No.	Taxpayer (Appellee)	Collector (Appellant)	Fiscal Year Ended May 31
7488	The St. Helens Petroleum Co., Ltd.	Galen H. Welch	1921
7490	" " " " "	" "	1922
7493	" " " " "	Rex B. Goodcell	1922
7491	The Kern River Oilfields of Cal., Ltd.	" " "	1923
7492	" " " " "	" " "	1924
7489	" " " " "	" " "	1925

Dockets 7490 and 7493 involved the same taxpayer, the same taxable year, and the same issues, with separate suits being brought and separate judgments being rendered against two successive collectors of internal revenue because a part of the tax in controversy was paid to each of them.

The issue involving the deductibility of British income taxes is involved in *all* of these cases and was the only issue presented by the parties at the trial below, the other issues raised by the pleadings having been conceded by appellants in the stipulations filed at the trial. [R. 29-32, 38-39.]

The other issue, involved only in Docket Nos. 7488, 7490, and 7493, is the jurisdiction of the trial court to enter judgment in any case where the profits taxes have been determined under Section 328, Revenue Acts of 1918 and 1921. As Congress did not impose any profits tax for any period after December 31, 1921, this issue naturally is not presented in Docket Nos. 7489, 7491 and 7492.

Appellants have presented their full arguments on both issues in the brief filed in Docket No. 7488, and have merely referred to said brief in the briefs presented in all other cases. As a matter of convenience and to avoid confusion, the same procedure is being followed by appellees. Accordingly the full statement of argument on both issues will be presented in the brief filed under Docket No. 7488.

SUMMARY OF ARGUMENT.

Issue I. The Court below did not err in denying appellant's motion in arrest of judgment. Neither in the pleadings nor at the trial of the case was any issue raised as to jurisdiction of the Court or as to the propriety of the Court redetermining the profits tax on the basis of the rates previously determined by the Commissioner. Appellant conceded at the trial that the taxable net income of appellee had been overstated in the amount of $18,604.41 because of insufficient allowances for depletion deductions, and submitted to the Court for determination the propriety of an additional deduction of $41,553.05 for taxes, which issue was decided by the Court in favor of appellant. The total reduction in net taxable income found by the Court ($60,157.46) was small in comparison with the net income determined by the Commissioner ($2,350,422.78) and in the absence of any allegation or proof to the contrary, the Court was justified in applying to the correct net income the profits tax rates previously determined by the Commissioner. The Court has not attempted to override the discretionary powers of the Commissioner.

None of the authorities cited by appellant support his position and, on the contrary, the Supreme Court has in three cases affirmed, either in whole or in part, decisions of lower courts allowing refunds to taxpayers whose profits taxes had been determined under "special assessment."

Congress has not given the Commissioner unreviewable discretion where errors were admittedly made in the determination of net income, even though the profits taxes are computed under Section 328. This is particularly so in the case of foreign corporations to whose returns "special

assessment" was required by law and not granted as a matter of relief.

Even if the Commissioner's computation of the *profits tax* was not subject to review by the Court, such inhibition would not apply to the redetermination of the *income tax,* where the exact rate was provided in the law and was not a matter of discretion.

Under appellant's construction, the law would be of doubtful constitutionality. Since appellee's profits taxes had to be determined under "special assessment," it would follow under appellant's contentions that it could *never* obtain a judicial review of the Commissioner's determination of either its income or its profits tax, no matter how arbitrary or erroneous the basis. This would not only violate the due process clause of the Constitution, but would also amount to a delegation of legislative and judicial functions to the executive branch. The interpretation of the law adopted by the Court below avoids these constitutional difficulties and carries out the clear intention of Congress to provide a complete system of judicial review to taxpayers.

Issue II. Under the Federal Revenue Acts of 1918 and 1921, the deduction for taxes (including income taxes paid to a foreign Government) is allowable to the one on whom the taxes were imposed and by whom they were paid. It has been stipulated and found by the Court that the British income tax of $41,553.05, in issue here, was paid to the British Government by the appellee. [R. 31.] It is clear that, under British law, this tax was imposed on appellee, was determined on the basis of its net income, and was payable in any event, even though no dividends might ever be declared to its shareholders.

There is no British income tax on dividends as such. In paying the British income tax, appellee did so as a taxpayer and not as an agent for its shareholders. The mere fact that it was permitted, though not required, under the British practice, to deduct from dividends paid, if any, a proportionate amount of the tax, does not change the fact that it paid the taxes on its own behalf as a taxpayer. Such deductions from dividends did not result in any reimbursement to appellee of its own income tax payment; having paid the tax, its income available for dividends was merely the lesser sum.

To speak of the payment of the income tax by appellee as a "withholding" is simply a misnomer contrary to facts. It was required to pay the tax to the British Government on *its* entire net income even though (1) it made no payment whatever to its stockholders and (2) the stockholders had no income from this or any other source.

The construction contended for by appellant would result in confusion in the administration of our tax laws and often would result in an unfair and unjust duplication of deductions, defeating the collection of tax revenues.

The statute is plain and unambiguous, leaving no need for departmental construction. There has been no uniform and long continued rule of construction by the courts, the Board or the Treasury Department. The informal Bureau rulings relied upon by appellant "have none of the force or effect of Treasury decisions and do not commit the Department to any interpretation of the law." As a matter of fact, the Bureau's views on this question have changed from time to time. At the present time the Department is contending in various cases before the Board precisely in accordance with appellee's contentions herein.

ARGUMENT.

POINT I.

The Court Below Did Not Err in Denying Appellant's Motion in Arrest of Judgment.

As a foreign corporation, appellee's profits taxes for the year in question were determined under sections 327 (b) and 328, Revenue Acts of 1918 and 1921, through the method of comparison with the profits tax rates paid by representative domestic corporations, a determination usually referred to as "special assessment."

Appellee brought this suit in the court below to recover income and profits taxes "erroneously assessed and collected" by the appellant as collector of internal revenue.

The errors complained of were that whereas the law provides* that "in computing net income there *shall* be allowed" as deductions certain items, including depreciation, depletion and income taxes imposed by any foreign country, the Commissioner had in these instances refused to obey that provision, which leaves him no discretion. Issue was joined and the case was heard on the merits. At such hearing the appellant, represented by the United States Attorney, admitted that the Commissioner had erred as regards two of the deduction items mentioned in the petition (depletion and depreciation), and the trial court found in favor of the appellee as to these two items, and also as to the deductibility of an additional item of taxes which the petitioner claimed in the petition had been erroneously disallowed as a deduction.

---

*Sections 234(a)(7) and (9), Revenue Act of 1921.

The trial court, having found in favor of appellee, allowed the filing of an additional stipulation of facts. The appellant then filed a motion in arrest of judgment asserting (notwithstanding the errors admitted and the additional error found by the trial court), that judgment must be for appellant because the evidence was insufficient to enable the court to enter judgment for appellee, and further because the court lacked jurisdiction to enter judgment in favor of appellee.

The basis for the motion in arrest of judgment was that petitioner as a foreign corporation must have its profits taxes computed at rates arrived at by comparisons, to be made *exclusively* by the Commissioner of Internal Revenue, of appellee's gross and net income, with the gross and net incomes of other comparable business corporations, in the manner required by sections 327 and 328 of the Revenue Act of 1921*.

The evidence before the court when the motion in arrest of judgment was filed enabled the court to ascertain the profits tax rates theretofore determined by the Commissioner. It also showed what was appellee's gross income, its net income, and every factor necessary to enable the Commissioner to make the comparisons necessary to arrive at the proper profits tax rates to be applied to this correct net income. Appellant did not at any time aver (*and does not now aver*) that the proposed correction of net income would require the application of any different rates than those which the Commissioner of Internal Revenue found

*Under these sections, the profits tax is determined by applying to the statutory net income, calculated under Sections 232-236, Revenue Act of 1921, rates of tax determined by using as comparatives other corporations "similarly circumstanced."

to be applicable upon his original examination of the necessary comparatives.

The trial court denied the motion in arrest of judgment and entered a judgment in which (1) the ordinary corporation income taxes were calculated by applying the statutory income tax rates to the corrected net income, and (2) the *profits taxes* were calculated, for the years in which a profits tax was imposed, by applying to the corrected net income the profits tax rates originally determined by the Commissioner to be correct.

The trial court did not err in retaining jurisdiction of the case and in redetermining both the ordinary corporation income taxes and the profits taxes of appellee. Although the suit was against the Collector, he was represented by the United States attorney and counsel for the Commissioner. [R. 1, 14.] In addition, a certificate of probable cause was issued. [R. 25-26.] The court below was entitled, therefore, to assume from the failure of the defendant to plead that new profits tax rates were necessary, that the rates previously determined [R. 60] were appropriate for the corrected net income found by the court.

In any event, neither the Commissioner nor the United States will be concluded by the judgment against the Collector from protecting the interests of the United States.

Bankers Pocahontas Coal Company v. Burnet, 287 U. S. 308, 311-312;

Tait v. Western Maryland R. Company, 289 U. S. 621, 627.

(a) The Commissioner May Not Oust the Court of Jurisdiction by Failing to Advise the Court Whether or Not New Profits Tax Rates Are Required Because of the Court's Correction of Errors Made by the Commissioner in Determining Appellee's Net Income.

Appellant in this appeal appears to stand squarely upon the proposition that the Commissioner alone* has power to make determination of profits tax rates under sections 327 and 328 of the Revenue Act of 1921 and accordingly that the court below lacked jurisdiction to entertain the appellee's suit for refund, even though based on admitted errors in determining *net income,* as to which the Commissioner concededly has no discretion.

Thus, this appeal is based on a theory that the Commissioner's admitted errors in denying nondiscretionary deductions cannot be redressed in the United States courts because the Commisisoner's determination of the *excess profits tax* was a decision of a type which the courts will not review.

Appellee contends that there is no indication in any part of the tax law that Congress intended that errors made by the Commissioner in applying nondiscretionary parts of the tax law should not be reviewable by the courts, and particularly not in the case of foreign corporations who have no choice as to the application of special assessment. On the contrary, Congress intended to establish a system of remedial justice so that when the Commissioner assessed

---

*We have herein ignored the fact that the Board of Tax Appeals may review the determinations of the Commissioner respecting special assessment (*Blair v. Oesterlein Machine Company,* 275 U. S. 220), since that review may only be had where *additional* assessments are proposed by the Commissioner.

a tax in clear violation of definite provisions of the tax law, the taxpayer could recover a refund of the tax so erroneously assessed. If it is true that determinations *under certain paragraphs* of the tax law are within the discretion of the Commissioner and are not reviewable by the courts, it still remains true that when he misapplies one of the *nondiscretionary* provisions of the tax law, his error in that regard is intended to be reviewed by the courts. In this case, as has been pointed out, appellant has never alleged or proved that the Commissioner's determination of the *rate of excess profits tax* (said to be unreviewable in court) was wrong or was not properly applicable to the net income as now determined by the court.

Appellant's position is also untenable in that it fails to give effect to appellant's status as a party defendant in an action at law for a recovery of taxes "erroneously assessed or collected". District courts have been vested with jurisdiction of suits of this character, and the right to sue Collectors of Internal Revenue in cases of this kind has existed since the beginning of the National Government as a common law right carried over by our Government from colonial jurisprudence. *Sage v. United States,* 250 U. S. 33, 37; *United States v. Emeny etc. Co.,* 237 U. S. 28, 31. Such suits have been authorized as a part of a system of corrective justice in relation to the revenue laws so complete that Congress has been sustained in the enactment of statutes depriving taxpayers of injunctive relief from erroneous or illegal assessments. *Cheatham v. United States,* 92 U. S. 85, 88; *Snyder v. Marks,* 109 U. S. 189, 193; *Bailey v. George,* 259 U. S. 16, 20; *Graham v. Dupont,* 262 U. S. 234, 255. Being actions in assumpsit, they approach nearer to a bill in equity than any other

common law action. *American Chain Company v. Eaton,* 291 U. S. 386, 402; *Howbert v. Norris* (C. C. A. 10), 72 F. (2d) 753, 755; *New York Life Insurance Company v. Anderson* (C. C. A. 2), 263 Fed. 527, 530.

When made a party defendant in the suit at bar, the appellant had a right to rely upon a presumption that the tax assessment by the Commissioner was free from error (*United States v. Rindskopf,* 105 U. S. 418, 422; *Wickwire v. Reinecke,* 275 U. S. 101, 105), but when *prima facie* error was established (it was admitted in this case) and no reason appeared why the correct amount of the tax could not be found, the burden of next proceeding shifted to the appellant*. *Commissioner v. Van Vorst* (C. C. A. 9), 59 F. (2d), 677; *Duffin v. Lucas* (C. C. A. 6), 55 F. (2d) 786-796; *Jones v. Commissioner,* (C. C. A. 7), 38 F. (2d) 550; *Wilson v. Eisner* (C. C. A. 2), 282 Fed. 38, 42; *Bernheim Distilling Company v. Mayes* (D. C. Ky.), 268 Fed. 629-633.

In this connection, attention is invited to the decision of the Supreme Court in *Helvering v. Taylor,* January 7, 1935, holding that it was not necessary for the taxpayer to prove the correct amount of the tax where he has shown clear error in the Department's determination. The opinion states in part as follows:

> "Unquestionably the burden of proof is on the taxpayer to show that the Commissioner's determination is invalid. *Lucas v. Structural Steel Co.,* 281 U. S. 264, 271; *Wickwire v. Reinecke,* 275 U. S. 101, 105. *Welch v. Helvering,* 290 U. S. 111, 115. Frequently,

---

*There was certainly no reason why the trial court should assume as a matter of judicial notice that a decrease of appellee's net income (determined by the Commissioner to be $2,350,422.78) by only $60,157.46 would require the application of revised profits tax rates.

> if not quite generally, evidence adequate to overthrow the Commissioner's finding is also sufficient to show the correct amount, if any, that is due. See, *e. g., Darcy v. Commissioner*, 66 F. (2d) 581, 585. But, where as in this case the taxpayer's evidence shows the Commissioner's determination to be arbitrary and excessive it may not reasonably be held that he is bound to pay a tax that confessedly he does not owe, unless his evidence was sufficient also to establish the correct amount that might lawfully be charged against him."

If the new and correct net income required a determination of new rates for the profits tax, the *duty* of showing such requirement and what were these new rates, devolved upon appellant. Nor is this duty affected by the circumstances that the court may have lacked power to revise any rates determined by the Commissioner "in the absence of fraud or other irregularities". (*Williamsport Wire Rope Company v. United States*, 277 U. S. 55.) Neither appellant nor the appellee made any claim in the court below that the change in appellee's net income required any redetermination of profits tax rates under the procedure prescribed by sections 327 and 328 of the statute and neither *has since contended* that such revisions of rates are required as a matter of fact. In these circumstances the trial court properly concluded that the rates previously determined by the Commissioner were appropriate to be used in connection with the revised net income of appellee.

Appellant appears to contend that because a revision of profits tax rates *might* conceivably be required, and because the normal tax *might* also be affected, the trial court lacked *jurisdiction* to continue with the case.

That there is no inherent lack of *jurisdiction* is made plain by considering that if the appellant had voluntarily stipulated the correct profits tax rates applicable to the corrected income, no impediment to full correction of the Commissioner's refusal to allow deductions, mandatory under the law, would have existed, even under appellant's theory of the case. Compare *United States v. Factors and Finance Company,* 288 U. S. 89.

Appellant's contention, in its basic form, is evidently that the Commissioner not only has exclusive discretion in arriving at the correct *profits tax rates* to be applied in the case of a foreign corporation, but also has such unreviewable discretion so to act that the courts are unable to correct errors admitted to have been made by him in determining justiciable matters, such as deductions allowable in determining net income.

Such unreviewable discretion (as regards errors in determining net income) as appellant seemingly claims has not been expressly granted to the Commissioner. Its existence would be at complete variance with the long established system of corrective justice expressly provided for by Congress. The result obtained is so shocking to reason and justice, as to deny the imputation to Congress of an intention (not expressed in the statute) to single out *foreign* corporations for such unfair treatment. Domestic corporations which voluntarily make application for special assessment as a matter of *relief* have an alternative which affords them a judicial review. See *Heiner v. Diamond Alkali Co.,* 288 U. S. 502, 507.

(b) The Precedents Cited by Appellant do not Support His Contention.

In considering the precedents relied upon by appellant it should be borne in mind that appellee is a *foreign* corporation; that under the Revenue Act of 1921 (Section 327(b)) it is *mandatory* that its profits taxes be determined by the procedure prescribed in Section 328 of that statute; and that in this case no effort has been made to have the trial court review or revise in any degree any determination of the profits tax rates made by the Commissioner, pursuant to Section 327 or 328 of the statute. Appellee concedes that special assessment was mandatory and that the Commissioner's selection of representative corporations was correct. Nor was it necessary that any such review be had. All that was necessary was that the appellant tell the court the correct tax rates to be used, if any change in the profits tax rates was found necessary as a result of the reduction in income. It has never been alleged in this case that the correction of the net income required any redetermination of the profits tax rates, and in the absence of such allegation or showing, the trial court was fully justified in assuming no change was necessary.

In each of the cases relied upon by appellant some interference, direct or indirect, with the exercise of the Commissioner's discretion was necessary to a determination of the issues before the courts. All of these cases, with a single exception, related to *domestic* corporations and directly involved the exercise of two discretionary powers reposed with the Commissioner; (a) the determination whether special *relief* under Section 328 was justified, and (b) the selection of proper profits tax rates through

the use of comparatives (i. e., corporations similarly situated as to business and gross and net incomes).

In *Williamsport Wire Rope Company v. United States,* 277 U. S. 551, a *domestic* corporation sought a review in the Court of Claims of a refusal by the Commissioner to grant special relief under Sections 327(d) and 328 of the Revenue Act of 1918 because of alleged abnormalities in the relationship of plaintiff's net income to its gross income. The Supreme Court reviewed the nature of "special assessment" authorized by these sections as an alternative "relief" procedure to be availed of in appropriate cases upon application by the taxpayers, and concluded that Congress had not meant to empower courts to grant this relief where the Commissioner had determined that it was not appropriate. The Court affirmed the action of the Court of Claims in sustaining a motion to dismiss the proceeding.

In *Heiner v. Diamond Alkali Company,* 288 U. S. 501, the plaintiff, a *domestic* corporation, sought special assessment because of alleged abnormalities which entitled it to special relief under Sections 237(d) and 328 of the Revenue Act of 1918. The Commissioner granted "special assessment." The plaintiff sued for a refund in the District Court, alleging errors by the Commissioner both as to the amount of its net income and *as to the rates of profits taxes* arrived at by the Commissioner through the procedure prescribed by Section 328 of the statute. The trial court found (39 F. (2d) 645) that the Commissioner had erred in arriving at the plaintiff's net income, and applied the profits tax rates determined by the Commissioner. The Circuit Court of Appeals for the Third Circuit (60 F. (2d) 505) found that the Commissioner had erred to a greater degree than found by the trial court in arriving

at the plaintiff's net income, and held that the profits tax rates originally determined by the Commissioner should be applied to this corrected net income.

On appeal by the Collector, the Supreme Court pointed out that the plaintiff had deliberately sought special assessment; that the granting thereof by the Commissioner was a discretionary power vested solely in him; and that the correct amount of net income was an essential factor in the Commissioner's discretionary determinations (a) whether special assessment was warranted and (b) what comparatives should be used in fixing the correct profits tax rates. Upon these considerations the Supreme Court held that the lower courts had erred in proceeding as had been done. The Supreme Court did not decide, however, that the courts lacked jurisdiction of the case merely because special assessment was involved, but remanded the case for "further proceedings in accordance with this opinion." As a matter of fact, the lower courts had revised the amounts of both the income tax and the profits tax. The Government did not question on appeal to the Supreme Court the reduction of the normal income tax so a refund was actually allowed in that case. Obviously, if the courts have no jurisdiction of cases in which special assessment has been applied, the Supreme Court would have directed the lower courts to dismiss the whole proceeding.

In *Brown's "Shamrock" Linens, Ltd. v. Bowers,* 48 F. (2d) 103, the plaintiff, a *foreign* corporation, brought suit in the District Court for a refund on the ground that the Commissioner had used improper comparatives in determining the plaintiff's profits taxes pursuant to Sections 327(b) and 328 of the Revenue Act of 1918. The Col-

lector's motion to dismiss was granted by the District Court (4 F. (2d) 862) and the Circuit Court of Appeals for the Second Circuit affirmed. That court, however, made it plain that its decision was limited to a case (unlike the case at bar) where a court was asked to substitute its judgment as to proper comparatives for tax rate purposes for the judgment of the Commissioner. The court said:

> "The fact that special assessment is mandatory for a foreign corporation and permissive for a domestic one furnishes no basis for distinction *when each is attacking the Commissioner's computation on the ground that he selected improper comparatives in determining the assessment which he made.*" (Italics supplied throughout this brief.)

This decision seems open to serious question on constitutional grounds, and although *certiorari* was denied by the Supreme Court (283 U. S. 865), it cannot be regarded as reflecting the views of that Court. *United States v. Carver,* 260 U. S. 482, 490. Note also the dissenting opinion of Circuit Judge Manton at 48 F. (2d) 104-105.

Moreover, the facts in that case are essentially different from those in the case at bar. In that case there was no error in the determination of the net income and the Court could only grant relief by making a new "special assessment" in substitution for that made by the Commissioner. In the case at bar errors were made as to the correct net income of the plaintiff—plainly a justiciable matter—and relief was not dependent upon any revision by the court of the "special assessment" determination of the Commissioner.

Duquesne Steel Foundry Steel Foundry Company v. Commissioner, 41 F. (2d) 995; *Cramer and King Company v. Commissioner,* 41 F. (2d) 24; and *Railroad Supply Company v. Burnet,* 51 F. (2d) 437, each involved efforts to have the courts review decisions by the Board of Tax Appeals which affirmed decisions by the Commissioner that the petitioners (*domestic* corporations) were not entitled to relief by special assessment. These cases were substantially identical, therefore, with *Williamsport Wire Rope Company v. United States, supra.*

Joseph Joseph & Bros. Company v. United States, 71 F. (2d) 389; and *Chicago Frog & Switch Company v. United States,* 67 Ct. Cls. 662, involved suits for refunds in which *domestic* corporations alleged that the Commissioner erred in the comparatives selected for rate determinations under "special assessments" sections of the statute and were directly controlled by *Williamsport Wire Rope Company v. Commissioner, supra.*

In *Cleveland Automobile Company v. United States,* 70 F. (2d) 365, a *domestic* corporation, sought and secured special assessment, and thereafter brought suit in the District Court alleging errors in determination of its net income as determined by the Commissioner. Judgment was for the Government and on appeal the Circuit Court of Appeals for the Sixth Circuit affirmed. That court pointed out that the facts were substantially those involved in *Heiner v. Diamond Alkali Company, supra,* in that a revision of the net income would entitle the Commissioner to reconsider whether or not special relief was justified and, if so, what profits tax rates should be

used. The court did not, however, remand the case for further proceedings as did the Supreme Court in the *Diamond Alkali Company* case, but found, *on the merits,* that the net income had not been overstated.

Central Iron and Steel Company v. United States, 6 F. Supp. 115; and *W. H. Bradford and Company v. United States,* 6 F. Supp. 117, were cases involving *domestic* corporations in which special assessment was allowed by the Commissioner and refunds were sought in the Court of Claims on allegations that the Commissioner had erroneously determined the net incomes of the plaintiffs. The Court of Claims pointed out that these facts were the same as were involved in *Heiner v. Diamond Alkali Company, supra,* but dismissed the suits instead of requiring the Commissioner to show whether special assessment was warranted and the correct rate of tax, based upon the correct net incomes. The dismissals in these cases may have been appropriate, owing to the limited jurisdiction of the Court of Claims which (unlike a District Court) may not require taxing officials to proceed with affirmative defenses upon penalty of having judgment rendered against them. However, these decisions by the Court of Claims are inconsistent with other decisions of that court.

In *United States v. Supplee-Biddle Hardware Co.,* 265 U. S. 189, affirming a decision of the Court of Claims, 58 Ct. Cls. 343, "special assessment" had been granted by the Commissioner and yet the Supreme Court affirmed a refund of both income and profits taxes ordered by the lower court. Obviously, if the courts have no *jurisdiction* in special assessment cases, the Supreme Court, which

noted the fact that the profits taxes had been computed under Sections 327 and 328 of the Revenue Act of 1918 (pp. 193-194), would have ordered that the proceeding be dismissed.

In *Factors and Finance Company v. United States*, 73 Ct. Cls. 707, 56 F. (2d) 902, the plaintiff, a *domestic* corporation, filed a refund claim alleging that the Commissioner had erred in matters relating to its net income. After the statute of limitations on filing refund claims had expired, but while the Commissioner still had the claim for refund under consideration, plaintiff filed an amended claim for refund seeking relief by special assessment. The Commissioner examined all of the facts and made a tax determination under the special assessment section of the statute (Section 210, Revenue Act of 1917), but refused to make a refund of the over-assessment admitted by him to have been made, on the theory that the amended refund claim was in fact a new claim which was barred by the statute of limitations. The plaintiff sued for relief in the Court of Claims, which gave judgment for the refund due under the Commissioner's special assessment. The Supreme Court affirmed the judgment of the Court of Claims. (*United States v. Factors and Finance Company*, 288 U. S. 89.)

In *Oak Worsted Mills v. United States*, 38 F. (2d) 699, the Court of Claims sustained the right of the Commissioner to exact an additional tax from a domestic corporation by way of a second "special assessment" within the period of limitations upon assessments and collections. The court did not conclude in that case that it had no jurisdiction (see opinion by Judge Littleton), but retained jurisdiction and entered a judgment which made the issues *res judicata* as between the parties.

In *Freeport Texas Company v. United States,* 58 F. (2d) 473, the Court of Claims again took jurisdiction of a refund suit deciding it upon the merits against the *domestic* taxpayer, observing incidentally that since special assessment had originally been sought and secured the court believed that the plaintiff could not in a later proceeding seek to have the taxes computed on a different basis.

United States v. Henry Prentiss & Company, 288 U. S. 73 and *McDonnell v. United States,* 59 Fed. (2d) 290, each involved the applicability of statutes of limitations to suits for refunds by *domestic* corporations, and are not here in point.

In *U. S. Paper Exports Ass'n v. Bowers,* 6 F. Supp. 735, the District Court assumed jurisdiction and ordered a refund in a case where special assessment had been granted to a *domestic* corporation.

(c) The Question of Jurisdiction Would in Any Event Apply Only to the Profits Taxes and Not to the Income Tax.

Under the Revenue Acts of 1918 and 1921, here in question, corporations were subjected to two entirely different types and amounts of taxes, as follows:

(1) Under "Title II—Income Tax," an *income tax,* computed on a straight and fixed percentage of the taxable net income.

(2) Under "Title III—War Profits and Excess-Profits Tax," a *profits tax,* computed under one of the following methods, the lowest tax shown to prevail:

(a) Under Section 301, the normal method for *domestic* corporations, requiring different rates and

depending for credits and brackets upon the statutory "invested capital." This method was expressly not available to *foreign* corporations.

(b) Under Section 302, providing a maximum "limitation of tax," computed without reference to invested capital but with different rates and brackets. This method also was not available to *foreign* corporations.

(c) Under Section 328, computed with reference to the rates of profits taxes paid by "representative corporations," similarly circumstanced. This method was applied to such *domestic* corporations only as qualified for same, within the discretionary determination of the Commissioner, under the terms of Section 327. Under Section 327(b), however, the Commissioner was *required* to apply this method of computation to all *foreign* corporations.

It should be noted that the law required the profits taxes of appellee, as a foreign corporation, to be determined under Section 328. There was no alternative option to such a corporation, even though it might have a large and useful invested capital; and likewise the Commissioner had no choice or discretion regarding the applicability of "special assessment."

The taxes paid by appellee for the taxable year in question and the taxes sought to be recovered in this proceeding, consisted not only of profits taxes assessed under Section 328, but also of *normal income taxes which were computed and assessed under an entirely different title of the Acts without any reference whatever to Section 328.*

In *Heiner v. Diamond Alkali Co., supra,* the Supreme Court held that, in the case of a *domestic* corporation, the courts could not alter or revise the Commissioner's com-

putation of the *profits tax* under "special assessment." However, no appeal was taken by the Government from, and no decision was rendered by the Supreme Court with respect to, the revision by the lower courts of the *income tax*. On page 12 of the Solicitor-General's brief before the Supreme Court in that case appeared the following statement:

> "Petitioners do not question here the action of the courts below in reducing the *normal income tax* by increasing the deductions from gross income and applying to the reduced net income the normal tax rate prescribed by the statute. The questions presented to this Court in the instant cases relate only to *profits taxes*. Attention, however, is called to the fact that there is a necessary correlation between the profits tax and the income tax since, under Sec. 236(b) of the statute, the amount of the former is allowed as a credit against net income in computing the latter."

Accordingly, while the question was not decided by the Supreme Court, the *Heiner v. Diamond Alkali Co.* case would appear to be strong authority for the proposition that, even in the case of a domestic corporation, the courts have jurisdiction to correct errors in the computation of income and to revise the *income tax* on the basis of such corrected net income, even though the *profits tax* had been determined under special assessment.

As a matter of logic, this would appear to be the correct procedure. If the courts are without power to revise the amount of profits tax determined by the Commissioner, it follows that such determination reflects the correct and final amount of the profits tax due and payable, and as such is a proper deduction in computing net income, for purposes of the income tax.

Clearly, the Commissioner has been given no discretionary power with respect to the *income tax* computation, which is at a fixed rate prescribed in the statute. Accordingly, where, as here, the Government concedes or the courts find that the Commissioner has erroneously overstated the taxable net income, there is no reason, in logic or in fairness, why the fixed rate should not be applied to the corrected net income. Obviously, such determination requires no comparison with Departmental data on other corporations and presents no practical or administrative difficulties to the courts.

Accordingly, we submit that irrespective of this Court's decision with respect to the trial court's revision of appellee's profits taxes, no error was committed in redetermining the income tax on the basis of the net income as determined by the Court.

(d) The Statute as Construed by Appellant Would Be of Doubtful Constitutionality.

Appellant apparently contends that Congress has vested the Commissioner with the power to determine the profits tax rates which are to be applied to foreign corporations, and the power to make these findings without any right of review by the courts.

The fixing of tax rates is a function of Congress (Art. I, Sec. 8, United States Constitution), and it may well be questioned whether the general standard by which the Commissioner is to act has been sufficiently delineated so as to prevent the statute from being a delegation of legis-

lative authority vested solely in Congress by Article I, Sections 1 and 8, of the Constitution.

United States v. Merriam, 263 U. S. 179;
United States v. Cohen Grocery Co., 255 U. S. 81;
Field v. Clark, 143 U. S. 649-700;
Yick Wo v. Hopkins, 118 U. S. 356-374;
Panama Refining Co. v. Hopkins, decided by Supreme Court Jan. 7, 1935, Vol. 79 L. Ed. 223.

By eliminating all review by the courts, even as to the determination of gross and net income (in appellant's view of the law), Congress would seem, in so far as *any* review by the Commissioner of his own acts is concerned, to have delegated purely judicial functions to an administrative officer in violation of Article III, Section 1, of the Constitution. See:

Phillips v. Commissioner, 283 U. S. 589-595 *et seq.;*
Kilbourne v. Thompson, 103 U. S. 168;
Monangehela Navigation Co. v. United States, 148 U. S. 312;
Murray's Lessee v. Hoboken Land and Improvement Co., 59 U. S. (18 How.) 272.

There is nothing in the statute which expressly requires the Commissioner to hear appeals by foreign corporations from tax determinations made by the Commissioner, and unless the same rules apply as in other and admittedly justiciable cases, the property of these corporations may be taken from them without due process of law in violation of the Fifth Amendment to the Constitution. Taxation by fiat, whether by Congress or an executive officer, is unconstitutional.

Heiner v. Donnan, 285 U. S. 312;
Schlesinger v. Wisconsin, 270 U. S. 230.

This is true even if Congress could be regarded as having a motive or policy to regulate or discourage the activities of foreign corporations, which is very doubtful.

Child Labor Tax Case, 259 U. S. 20;
Hill v. Wallace, 259 U. S. 44.

Even if it be considered that Congress by granting the Commissioner power to make reasonable and proper regulations, intended that foreign corporations would be granted a right of appeal to the Commissioner—it is quite plain that the Commissioner is not required to disclose the basis upon which he made his determinations so that such an appeal would be worthless and not due process of law. A taxpayer cannot present his case if he does not know what facts the Commissioner has relied on.

The statute, in appellant's view, forecloses judicial review of any tax determinations made by the Commissioner, in respect of foreign corporations, even where, as here, the Commissioner admittedly made errors in the computation of net income, the base for the tax. If such a provision were in the law, it would be so arbitrary and unreasonable as to amount to an authorization of confiscation of properties in the guise of getting taxes, and would for that reason also violate the Fifth Amendment.

Nichols v. Coolidge, 274 U. S. 531;
Eisner v. Macomber, 252 U. S. 189;
Hoeper v. Tax Commissioners, 284 U. S. 206;
Klein v. Board of Tax Supervisors, 282 U. S. 19.

It is a well recognized principle of statutory construction, that the courts will avoid, where possible, giving to a statute any interpretation which will cast doubt upon its constitutionality.

Strattons Independence v. Howbert, 231 U. S. 399.

POINT II.

The Court Below Did Not Err in Holding That Appellee Was Entitled to the Deduction of Income Taxes Paid by It to Great Britain.

Preliminary Statement. The appellee, St. Helens Petroleum Company, Ltd., being organized under the laws of Great Britain, and being a resident of that country, was subject to the British income tax on its entire income from all sources, 99.75 per cent of which was derived in the United States during the fiscal year ended May 31, 1921. [R. 31.] Likewise, the United States Government imposed income and profits taxes upon the portion of appellee's income which was derived from sources within the United States. Thus it was that appellee's income from United States sources was subject to both British and United States income and profits taxes.

Our revenue acts have consistently allowed a deduction for income taxes paid to a foreign country in determining the net income subject to our tax. (Sec. 234 (a) (3), Revenue Acts of 1918, 1921, 1924 and 1926; Sec. 23 (c) (2), Revenue Acts of 1928, 1932 and 1934.) This allowance is subject to certain limitations as to amount, based upon the sources of the income on which the foreign tax was imposed, but there is no question as to such limitations in the present case. The parties have stipulated that the amount deductible, if at all, is $41,553.05. [R. 31.]

The only issue involved in the present case is whether the appellee is to be deprived of the deduction because of the fact that it deducted an amount equivalent to the British tax from dividends paid to its shareholders.

(a) Under Our Revenue Acts the Deduction for Taxes Is Allowable to the One on Whom the Taxes Were Imposed and by Whom They Were Paid.

Section 234 (a) (3), Revenue Acts of 1918 and 1921, provide as follows:

> "(a) That in computing the net income of a corporation subject to the tax imposed by Section 230 there *shall be allowed as deductions:*
>
> "(3) Taxes *paid* or accrued within the taxable year except (a) income, war-profits, and excess-profits taxes imposed by the authority of the United States, (b) so much of the income, war-profits and excess-profits taxes imposed by the authority of any foreign country or possession of the United States as is allowed as a credit under Section 238, * * *."

The test of deductibility of taxes under the above section, and the similar sections of later acts, as disclosed by the decided cases, is "imposition" and "payment".

In *Shearer v. Commissioner,* 48 F. (2d) 552, the purchaser of an automobile who had been billed for the excise tax on the sale claimed the right to deduct that tax. The Circuit Court of Appeals for the Second Circuit, in an opinion by Judge Learned Hand, pointed out that the tax was imposed on the dealer, and could not be deducted by the purchaser, even though he ultimately bore the burden of the tax. On this subject the opinion states—

> "But the final incidence of taxation is not a measure of the person on whom the tax is levied, and it seems to us that the form of the statute must control. * * *"

Decisions of the Board of Tax Appeals of like effect are:

Appeal of R. C. Musser, 3 B. T. A. 498;
Hamilton v. Commissioner, 6 B. T. A. 240.

In these cases, deduction for the excise tax on automobiles was denied the purchasers, though they had been separately billed for the tax by the dealers. The ground for the decisions was that the tax was not imposed on the purchasers.

In *Small v. Commissioner,* 27 B. T. A. 1219, the Board denied a deduction for taxes paid by a husband on property belonging to his wife, although the husband had obligated himself to the mortgagee to pay taxes on the property. The Board's opinion reads in part as follows:

> "In order to be entitled to a deduction for taxes paid, a petitioner before us must show not only that he paid the taxes, but that the taxes were *imposed upon him* by the taxing authority. *A. Eisenberg,* 11 B. T. A. 574; *Samuel Riker, Jr.,* 15 B. T. A. 1160; *Caroline T. Kissell,* 15 B. T. A. 1270; *George L. Shearer,* 18 B. T. A. 465; affd. in *Shearer v. Commissioner,* 48 Fed. (2d) 552; *Falk Corp.,* 23 B. T. A. 883; aff'd. 60 Fed. (2d) 204; and *Borg & Beck Co.,* 24 B. T. A. 995. The petitioner has not shown that the taxes in question were *imposed upon him.*"

In *Peterson v. Commissioner,* 31 B. T. A. 172, the petitioner received a certain sum as a prize in a lottery, less his share of an income tax assessed by the Government of Newfoundland against the organization which conducted the lottery. The petitioner claimed the deducted tax as a credit against his United States tax on

the lottery prize. The Board denied the credit, its opinion reading in part as follows:

> "The imposition upon and the payment of the tax by the organization conducting the lottery would necesarily reduce the proceeds from the lottery out of which prizes could be paid. This in turn would reduce the amount that would be received by winning ticket holders. But these facts in and of themselves would not make the tax paid by the organization a tax upon the winning ticket holders. *For a foreign tax paid to be allowable as a credit against a taxpayer's Federal income tax liability, such foreign tax must have been a tax against the taxpayer and not a tax imposed upon and paid by another on its own account, as was the situation in the instant case. Elgin National Watch Co.,* 17 B. T. A. 339; *Basil Robillard, Executor,* 20 B. T. A. 685; *Duckworth Co.,* 24 B. T. A. 304."

Bureau rulings on this subject are—

A. R. R. 3041, C. B. II, page 1100—holding that the sales tax imposed by Section 902, Revenue Act of 1918, could not be deducted by the vendee even though he reimbursed the vendor for the tax.

A. R. R. 1020, C. B. I-2, page 104—denying the trustee under a will the right to deduct Federal estate taxes paid by them.

We do not understand the statements which appear at pages 10 and 11 of the appellant's brief to the effect that the gasoline tax is deductible by the purchaser of gasoline. Mim. 3988, C. B. XI-2, 25, holds that the Federal Gasoline Tax imposed by Section 617, Revenue Act of

1932, is deductible by the manufacturer, producer or importer. This ruling states—

> "* * * A jobber, dealer, or consumer who reimburses the manufacturer, producer, or importer for such taxes, even though billed to him as a specific item, is not entitled to deduct from gross income the amounts so reimbursed * * *."

Likewise, in *G. C. M.* 7630, C. B. IX-2, 107, the General Counsel ruled that "the motor vehicle fuel tax imposed by the State of California is deductible for Federal income tax purposes by the distributor who pays it and not by the consumer".

While the point is not raised in appellant's brief, mention should be made of the argument in the *amici curiae* brief filed in this case, to the effect that appellee is to be denied the deduction for British income tax because it has subsequently "recouped" same from its stockholders. This argument apparently proceeds on the theory that the corporation, while entitled to the tax deduction, realizes taxable income through the subsequent "reimbursement". The answers to this argument are as follows:

(1) As will be demonstrated later in this brief, no recoupment or reimbursement is involved. The corporation merely deducts the tax from its income and pays the remainder in dividends to its shareholders.

(2) The corporation has already satisfied its tax liability to the Crown, so its liability is in no sense satisfied by its shareholders.

(3) The corporation is not enriched through the payment of dividends to its shareholders, whether or not the dividend is "free of tax". It receives nothing from

them. What has happened is that the corporation has paid to its shareholders exactly what it was obliged to pay them under the dividend resolution, no more and no less. *Cf. Commissioner v. Rail Joint Co.,* 61 F. (2d) 751 (C. C. A. 2.) If, for example, the corporation declared as dividends the whole of its surplus, leaving it with its original capital and nothing more, in what form would the alleged income be?

(4) Even if the appellee realized taxable income through "recoupment" of its British income tax by deduction from dividends paid to its shareholders, such income was derived entirely from a transaction in Great Britain and to no extent from sources in the United States. Accordingly, such income would not be subject to taxation in the United States. See Section 233(b), Revenue Acts of 1918 and 1921.

Accordingly, since the tax in question was imposed upon and measured by the income of appellee and was actually *paid* by it, it is deductible from its taxable net income under the clear provisions of our law. As stated in the opinion of the Court below:

> "The foreign corporation in the express language of the Revenue Act is entitled to a deduction of such payments and I regard as entirely incidental the circumstance that under the laws of the foreign country the corporation is entitled to credit to the tax so paid when it comes to paying dividends to its shareholders. The interpretation sought by the government would change a provision of a statute in which there is no ambiguity whatever. This may not be done. (Gould v. Gould, 245 U. S. 151.)"

(b) Under the British Law the Tax Here in Question Was Imposed on and Was Paid by the Appellee.

The appellant has stipulated that the income tax of $41,553.05 was paid to the British Government by the appellee [R. 31], and the Court below so found in its Special Findings of Fact [R. 21]. The following references to the British Revenue Act of 1918 will show that the above tax was imposed on the appellee *as a company income tax.*

Under the provisions of the British Income Tax Act of 1918, the company is the taxpayer whether the company pays its dividends less tax, or free of tax, the company being free to choose either method since Rule 20 is permissive. Rule 1 of the General Rules, applicable to Schedules A, B, C, D, and E, contained in the Income Tax Act of 1918, provides that:

> "Every body of persons shall be *chargeable* to tax in like manner as any person is chargeable under the provisions of this Act."

Section 237 of the Act, which is the interpretative section, defines "a body of persons" to mean (*inter alia*) "any company."

The provisions referred to are not ambiguous, and, were it not for Rule 20, the present controversy would not have arisen. The question, then, is whether this rule has the effect, when dividends are paid, and tax is deducted therefrom, of cancelling, or removing the imposition of a part of the tax that was imposed on and paid by the company.

(c) RULE 20 OF THE BRITISH ACT DOES NOT OPERATE TO CANCEL ANY PART OF THE INCOME TAX IMPOSED ON A BRITISH COMPANY, OR TO SHIFT ANY PART OF THAT TAX TO THE COMPANY'S STOCKHOLDERS.

For convenience, Rule 20 is quoted here, as follows:

> "The profits or gains to be charged on any body of persons shall be computed in accordance with the provisions of this Act on the full amount of the same before any dividend thereof is made in respect of any share, right or title thereto, and the body of persons paying such dividend *shall be entitled to deduct* the tax appropriate thereto."

It will be seen that the Rule is not mandatory, but is permissive only; also, that the Rule is not a tax imposing provision and that it does not direct the company which may elect to deduct tax from dividends to account therefor to the Crown.

It should be plain from an examination of Rule 20 that under the British system, as under our own system, it is recognized that dividends and the company profits out of which they are paid are economically the same income and since these profits bore income tax in the hands of the company, they are not again subjected to normal income tax when they come into the hands of the shareholders as dividends. Thus, we find when we come to examine the decisions of the British courts in cases which have involved Rule 20, that they have said:

(1) That a British corporation does not pay its own income tax as agent for its shareholders;

(2) That the company does not act as collector for the Crown when it deducts income tax from dividends, since,

(3) There is no income tax on dividends as such;

(4) That Rule 20 merely serves as a measure of surtax income and of the amount of relief due to shareholders who fall in the exempt class.

By way of an introduction to our examination of the decisions of the British Courts involving Rule 20, we quote from the opinion of Mr. Justice Rowlatt of the Court of the King's Bench, in the case of *Hamilton v. Commissioners of Inland Revenue* (1931), 16 British Tax Cases 213, cited in appellant's brief herein. Mr. Justice Rowlatt appears to have heard and decided a large number of the litigated tax cases in England in the court of first instance during the past ten or fifteen years and, as will be seen, his opinions are frequently quoted with respect and approval in the House of Lords. The *Hamilton* case will be discussed in detail later on. At present we quote from Mr. Justice Rowlatt's opinion merely for background against which to view the operation and effect of Rule 20 in the British taxing system. Mr. Justice Rowlatt said, in the *Hamilton* case (pp. 222-223):

> "Now, as I said during the argument, I do not think anybody has ever sat down to really tackle exhaustively, so as to work out a complete system, the problem which arises in relating the taxpayer's individual income to the income of the company. Those problems of course were very much in the background in 1842, but they came into some prominence as soon as you got the growth of the Joint Stock commercial companies, and their consideration has been one of the esoteric joys of the select company of Income Tax lawyers for a long time."

The statement just quoted, coming as it did, in 1931, from a British jurist who has probably had the widest experience with litigated tax cases of any British lawyer or judge, prepares us for the conflicting *dicta* in the British decisions as to the effect of Rule 20.

Rule 20 and its predecessor, Section 54 of the Revenue Act of 1842, have been in force for ninety-three years. It will fairly appear hereinafter, from citations of British decisions, that when this provision was first enacted, British companies were regarded as being no more than the aggregate of their shareholders, so that income tax levied upon corporations was thought of as being collected at the source from the shareholders. It will further appear that when, later on, the "corporate entity" theory became fully recognized in Great Britain, it became necessary to recognize also that the income tax paid by a corporation was paid on behalf of the corporation itself, and not on behalf of its shareholders. Still, Rule 20 remained in the British law, so, to square the "corporate entity" concept with other concepts which conflicted with the former, it was necessary for the British courts to indulge in a number of fictions. These fictions, which appear usually in the form of *dicta* in the earlier British decisions, have led the Bureau of Internal Revenue, and the appellant here, into error.

Thus, the appellant gives the impression throughout his brief that when a British corporation deducts tax from dividends, it does so as collector for the Crown, and actually remits the deducted tax to the Crown. This is not so. There is no British income tax on dividends, as such. Not one farthing of actual money changes hands when tax is deducted from dividends. The Crown gets but one income tax—that paid by the company on its

profits. All that happens when tax is deducted from dividends is a paper deduction. No income tax is paid to the Crown in respect of the dividend.

The concept upon which the tax is based is described by Mr. Justice Rowlatt in *Ritson v. Phillips,* 131 L. T. 384, 9 Tax Cas. 10 (1924), as follows:

> "He is not taxed on his dividends. The companies are taxed on their profits not as his agents (as has been loosely said), though at his ultimate expense. There is no provision for the return of any of this tax to the shareholder save in the process of giving effect to deductions and reliefs."

The British cases cited below point out that their law does not impose any income tax on dividends, as such; hence it follows there could be no occasion that would require (1) collection at the source by the company paying the dividend, or, (2) payment of any tax on the dividend by the shareholder; and, if there is no income tax on dividends, as such, it follows that the relief to dividend receivers who fall in the exempt class cannot be made on the theory that they paid an income tax on their dividends. The British cases are equally clear that the company does not pay its own income tax as agent for its shareholders.

In *Purdie v. Rex* (1914), 3 K. B. 112, 111 Law Times Reports 531, the contention was made by a married woman that she was entitled to a refund from the Crown of income tax deducted from dividends and interest paid to her by a company. She said that under Section 45 of the Act of 1842 she was exempt from tax, being a married woman living with her husband; that she had therefore been improperly taxed on her dividend by the process of

deduction under Section 54 of the Act of 1842, which was similar to Rule 20. Judge Rowlatt, of the Court of the King's Bench, denied Mrs. Purdie's contention for reasons which appear in his opinion, as follows:

> "Schedule D levies a tax on profits made from trade. In this case the trade is done by a company and Mrs. Purdie says 'I am one of the part-owners of the company.' How are we going to deal with income tax on profits made from trade when the trade belongs to a company? The answer is to be found in Section 54 of the Act of 1842. That says that a company shall make an estimate of its profits and gains computed on the amount of the profits and gains before any dividend shall have been paid, and that all persons entitled to dividends shall allow out of such dividends as a proportional deduction in respect of the duty so charged. *So that in effect the company is the taxpayer. There is strictly speaking no income tax on dividends at all. The company has to pay income tax on its profits as a company, and having paid income tax, the result is there is less to divide among shareholders.* That is what it comes to. Mrs. Purdie has, therefore, strictly speaking, never been charged with income tax at all in respect of her dividends from the company. What has really happened is that the company has been charged with income tax and is by so much the poorer, and has therefore to declare a smaller dividend. The company has been charged with the income tax and has to reimburse itself."

While the above decision was by a court of first instance, Mr. Justice Rowlatt's reasoning was quoted with approval by the House of Lords in the recent (1934) case of *Neumann v. Commissioners of Inland Revenue*, 150 Law Times Reports 481, 18 British Tax Cases 332.

Bradbury (Collector of Taxes) v. English Sewing Cotton Company, Ltd. (House of Lords, 1923), 8 British Tax Cases 481, involved this question. The taxpayer, a British company, owned all the stock of an American company and in the years 1914 to 1916 received dividends from the American company on that stock. During these years the American company, although incorporated in America, was controlled from England, hence, under British law it was resident in Great Britain and was subject to tax as a British company. In 1917 control of the American company was removed from Great Britain and it was not thereafter taxed as a British company. At the time this case arose, British companies were taxed on the average of their income for the three years preceding the year of assessment, and the question for decision was whether, in determining the English Sewing Cotton Company's taxable net income for 1917, it was proper to include therein the average of the dividends which it had received from the American company for the years 1914, 1915 and 1916. The Crown contended that the dividends were taxable as income received by a British company from a foreign source, whereas the taxpayer contended that the dividends were paid out of profits that had borne the British income tax and were not, therefore, again subject to income tax.

The Court of Appeal held with the taxpayer and its judgment was affirmed by the House of Lords. The following quotations are from the opinions rendered in the House of Lords:

Lord Wrenbury in his opinion (p. 516) said:

> "The English Sewing Cotton Company during the first three years held, and they subsequently continued to hold, all, or nearly all, the ordinary shares

in the American Company. They were entitled to receive, and did receive, dividends in respect of them. The fund available for their payment was not the profits of the American Company, but the differential sum remaining after deduction from those profits of the Income tax which the American Company was liable to pay and had paid. And the person to make payment to them was the American Company. The case was one within Section 54 of the Income Tax Act, 1842. The English Company as a holder of shares in the American Company was a person to whom an annual payment was made out of property of the American Company in respect of which the American Company was chargeable to Income Tax under the Act. The English Company could not, during the first three years, be assessed, and was not assessed, in respect of the dividends thus received. The American Company was the person, and the only person who could be assessed in respect of the profits of the business of the American Company. The corporator bore his share of the tax by the deduction of the appropriate share of the collective tax paid by the corporation from his dividend (Inland Revenue v. Blott (2), (1920), 1 K. B. 114, 130, 131)."

Lord Phillimore was of the same view. His opinion reads in part as follows:

"This case seems to depend upon the following considerations. A joint stock company is under the Income Tax Act, 1842, treated as a person and is directed to make a return of its profits or gains according to Schedule D upon a conventional figure, arrived at by taking an average of the three preceding years, and is liable to be assessed and taxed thereupon.

"If the principle of its being a distinct person, distinct from its shareholders or the aggregate of its shareholders, had been carried to a logical conclusion, there would have been no reason why each shareholder should not, in his turn, have to return as part of his profits or gains under Schedule D the money received by him in dividends. (p. 518.)

* * * * * * * *

"Be this as it may, I find no warrant in law for such a conception. *A company either comes under Section 40 of the Act of 1842, or it does not.* If it does not, it is not taxable; but in that event those who receive dividends from it will be taxable in respect of their dividends. *If it does come under Section 40, its shareholders are not taxable for their dividends.* This is so, not because of any implied rule of law against double taxation, a rule for which it would be difficult to find support in the books, but because dividends on shares in a taxed company do not come under Schedule D." (p. 520.)

Lord Justice Younger, of the Court of Appeal, afterwards Lord Blanesburgh, House of Lords, expressed the following views (pp. 501-502):

"Now during that period dividends upon its common stock were declared and paid by the American company. On these dividends, under Section 54 of the Act of 1842, Income Tax was deducted by the American company at its source. These dividends under that deduction were paid to the English company and they with its deducted income tax are the dividends with reference to which the present contention of the Crown is made.

"Now, there may, before Inland Revenue Commissioners v. Blott (supra), have been some ques-

tion as to the character in which these deductions of income tax were made by the American company. There is now no question upon that head. 'Plainly,' says Lord Cave in that case (125 L. T. Reports, 505; (1921) A. C. at page 201), 'a company paying income tax on its profits *does not pay it as agent for its shareholders. It pays as a taxpayer* and if no dividend is declared the shareholders have no direct concern in the payment. If a dividend is declared the company is entitled to deduct from such dividend a proportionate part of the amount of the tax previously paid by the company, and in that case the payment by the company operates in relief of the shareholder. But no agency properly so called is involved.'

"The same subject is dealt with, and in terms, for present purposes more directly in point, by Rowlatt, J., in his judgment in the same case (121 L. T. Rep. at p. 650 (1920), 1 K. B. at 130). The learned judge says: 'The dividends or drawings of corporators, shareholders, partners, joint-owners, and the like, were not again taxable as a new subject matter. Corporators or shareholders bore their share of the tax (*i. e., a share of the collective tax, not an individual tax*) from their dividends under the express authority of Section 54.' "

The views expressed in the opinions in the *Bradbury* case were noted and reaffirmed in 1934 by the House of Lords in *Neumann v. Commissioners of Inland Revenue,* 150 Law Times Reports 481, 18 British Tax Cases 332.

In the *Neumann* case, the taxpayer received a dividend that was paid out of profits that were theoretically charged with income tax in the hands of the company which paid the dividend, but which, actually, had not borne tax,, for the following reason:

The company which paid the dividend operated a property from which it received a rental income. The British law does not tax the actual rents received, but, instead, sets up a hypothetical income determined on the basis of an assumed rental value. The actual rents were considerably in excess of the assumed figure, and in a prior proceeding the Crown sought to tax the excess. The House of Lords there held that the hypothetical figure governed, regardless of the actual rents, and, after that decision the company distributed the excess rents as dividends to its shareholders. Neumann was one of these, and he received the sum of £4,275.

The Crown contended that, notwithstanding that the profits out of which the dividend was paid had not actually borne income tax in the hands of the company, for the purpose of the surtax, Neumann should report the sum received, of £4,275, plus the income tax "appropriate thereto" of £1,068 15s., making the amount subject to surtax £5,343 15s. The House of Lords held that only the sum received, £4,275, was subject to surtax.

The opinions in this case are of particular importance in that they:

(1) Approve the reasoning of *Purdie v. Rex, supra,* and *Bradbury v. English Sewing Cotton Company, supra.*

(2) The opinions disapprove the dicta in *Hamilton v. Commissioners of Inland Revenue,* cited on pages 38 and 50 of appellant's brief.

The opinion of Lord Tomlin states—

"The case is a difficult one, and the difficulty in part arises from the fact that the amendments from time to time made to the Income Tax Acts, directed as they frequently are to stopping an exit through the net of taxation freshly disclosed, are too often framed without sufficient regard to the basic scheme upon which the Acts originally rested.

"The relative positions of a company and the shareholders of the company in relation to Income Tax under the Income Tax Acts have always been recognized as special in character. It was never, I think, doubted that, under the Act of 1842, the profits of a business carried on by a company were taxable against the company under Schedule D, and were not taxable again, after distribution, in the hands of the shareholders under Schedule D or any other Schedule. At the same time, it was permisible to the company, under Section 54 of the Act of 1842, to deduct from the dividend the proportionate part of the tax paid to the tax collector, and the shareholders entitled to exemption from or abatement of Income Tax could, upon the footing of the deduction, obtain the necessary return of tax. I cannot but think that the position under the Act of 1842 upon its proper construction is correctly described in the following passage from the speech of Lord Phillimore in Bradbury v. English Sewing Cotton Company, Limited, (1923), A. C. 744, at page 769. * * *

* * * * * * * * *

"In practice, the matter did not work out quite so simply. It has to be remembered that the amount distributable in dividend in any year might, in view of the assessment of profits or gains under Schedule A being upon the basis of the average of the three

preceding years, as it then was, be much more or much less than the amount of the assessment for that year, so that if this proportionate deduction was treated as meaning the rateable proportion of the tax paid by the company in respect of the year of distribution, it might much exceed or be much less than the amount which would be deducted from the dividend if the current rate of tax in respect of the gross dividend had been deducted. At any rate, a practice seems to have grown up of companies deducting from dividends tax appropriate to the amount of the dividend at the current rate of tax, quite irrespective of the amount of tax paid by the company to the Revenue, and of the shareholders claiming exemption or abatement being treated by the Revenue as having paid tax to the extent of that deduction. *As the company making the deduction lay under no obligation to pay to the Revenue anything more than the tax based upon its own assessment, the result was that the tax returned to those claiming exemption or abatement could rarely, if ever, have had any exact relation to the amount of tax received by the Revenue from the recipient of returned tax.*

* * * * * * * * *

"The effect of this last-mentioned Section seems to place beyond doubt this, that, where tax may be deducted from a dividend, the amount deductible is the sum which equals the standard rate of tax for the year of payment upon the gross amount of the dividend and that, whenever the profits were earned, the sum from which the deduction is made, and the deduction itself, are to be treated as income and deduction in respect of the year in which the payment is made. *Thus, the deduction permissible from the*

dividend clearly had no relation to the figure of tax payable by the company to the Revenue, though there was still no obligation on the company to account to the Revenue for what was deducted. The deduction, in fact, was only part of a system by which was measured (1) the extent of the shareholder's right to have exemption or abatement, and (2) the liability of the shareholder to Sur-tax.

* * * * * * * * *

"I may say at once that, having regard to the view which I have expressed as to the general scheme and operation of the Income Tax Acts in regard to dividends, *I am unable to accept the view that dividends, as such, are taxable under Schedule D. I do not think they are.* I think it is accurate to say, as Mr. Justice Rowlatt said in *Purdie v. Rex* (1914), 3 K. B. 112, at page 116: 'There is, strictly speaking, no tax upon dividends at all.' They are, however, under Rule 20 of the General Rules and Section 39 of the Finance Act, 1927, and apart altogether from Section 7 of the Finance Act, 1931, liable, where the dividends are made out of profits or gains charged on the company, to sufficient deduction of a sum equal to tax at the standard rate on the gross amount of the dividends and, in such cases, the gross amount of the dividend is the Income Tax income to be taken into account, whether it be for computing the amount of tax which the shareholder is entitled to have returned, or for fixing his liability to Sur-tax. * * *"

Lord Wright's opinion reads in part as follows:

"Rule 20 is, in effect, based on Section 54 of the Income Tax Act, 1842, with the substitution of the words 'the tax appropriate thereto' for the words

'the tax proportionate thereto.' The scheme of these provisions, as I understand them, is to impose the tax on all the profits of the company at the source; if and so far as these profits have been so taxed, they are not liable to any further tax, other than sur-tax, in the hands of the shareholder receiving the dividend. *The shareholder and the company are, no doubt, separate entities; the company is not an agent for the shareholder to pay tax on the dividend, nor is the company the collector for the Revenue to deduct the tax from the dividend. The company is the taxpayer.* The shareholder has no right to any share of the profits till a dividend is declared; the company may use the profits in any way it pleases *vis-a-vis* any shareholder; it may put them to reserve or capitalize them or use them for extensions or improvements; the profits declared and paid as dividends in one year may have been made in previous years, when the standard rate of tax was different. It is only very rarely, and in exceptional cases, that dividends are paid out of any particular source of profit; usually they are paid out of the general revenue fund of the company. What is essential to the requirements of the Inland Revenue is that all the profits of the company should be taxed, and, if that is done, the Revenue is not concerned with what is done with these profits. *The company is not bound, but only authorised, to deduct tax in paying dividends;* whether it deducts or not is left to its discretion, because the profits, once having been taxed in the company's hands, do not bear further tax—apart from Sur-tax—in the shareholders' hands. There is, in fact, only one profit, no new profit being created from the fact that the shareholder gets his share; *the tax is a tax on the profits and not on the*

dividend. But, if tax is deducted from the dividend, the Acts have provided that it is to be at the standard rate of tax of the year of dividend, in order to avoid obvious difficulties which might arise because profits divided in one year may have been earned in other years. The provisions of Section 7 of the Finance Act, 1931, will be considered by me more particularly in connection with the cross-appeal.

"On a careful review of these provisions, I reach the conclusion that a shareholder is not separately taxable—I disregard Sur-tax—on a dividend, as a profit individual to himself, under Schedule D, Case VI, as the Court of Appeal held, or at all. Apart from what I conceive to be the clear effect of the Acts in this regard, I think the position has been so stated by this House more than once, at least as a matter of observation. Thus, in *Inland Revenue Commissioners v. Blott* (1921), 2 A. C. 171, at page 201, Viscount Cave thus explained the system:—'Plainly, a company paying income tax on its profits does not pay it as agent for its shareholders. It pays as a taxpayer, and if no dividend is declared the shareholders have no direct concern in the payment. If a dividend is declared, the company is entitled to deduct from such dividend a proportionate part of the amount of tax previously paid by the company; and in that case the payment by the company operates in relief of the shareholder.' In *Bradbury v. English Sewing Cotton Company* (1923), A. C. 744, at page 766, Lord Wrenbury thus expressed the same idea in concise form: 'The corporator bore his share of the tax by the deduction of the appropriate share of the collective tax paid by the corporation from his dividend.' Lord Phillimore expresses the same view at page 771: 'the share-

holder'—in the ordinary case of a taxed company—'is taken to have paid the tax upon his dividends through the company and is not . . . taxed upon them.'

"These cases, and other similar statements of the principle which I may quote, were, no doubt, made with reference to Section 54 of the Income Tax Act, 1842, but I do not think that the substitution in the later Act of the word 'appropriate' for the word 'proportionate' in the earlier Act, affects the principle. In 1842, the modern development of limited companies was not in contemplation; 'proportionate' was an apt word for the simple cases of corporators where each year the corporators shared, in definite proportions, the available net income. 'Appropriate' tax, which is more precisely defined by the Finance Act of 1927 as being at the standard rate of the year of payment, is clearly a more apt term in connection with the dividends of a company. But the same view has been expressed in regard to Rule 20 of the Act of 1918, for instance, by Lord Sterndale and Lord Warrington, in *Sheldrick v. South African Breweries, Limited* (1923), K. B. 173.

"The Court of Appeal, in deciding against the appellant, on the ground that the dividend he received was separately taxable in his hands at the standard rate (because charged with Income Tax under Schedule D), found some support for their decision in *Hamilton v. Inland Revenue Commissioners* (1931), 2 K. B. 495: in that case, the shareholder claimed that he was only liable to be taxed to the extent of a proportionate part—that is, in the proportion that a shareholding bore to the total issued capital of the company—and not on the basis of the

tax appropriate to his actual dividend. That contention was rightly rejected both by Mr. Justice Rowlatt and by the Court of Appeal. But the decision did not involve, or require, as I think, any conclusion that dividends were separately taxable in the shareholders' hands under Schedule D, nor did Mr. Justice Rowlatt so think, though certain dicta in the Court of Appeal may seem to point that way. I cannot, with respect, go with the Court of Appeal in dismissing the Appellant's appeal on the ground that the dividend, not being a capital distribution, was chargeable with Income Tax under Schedule D. For the reason I have stated, I think that is not in accordance with the provision of the Acts."

See, also:

Inland Revenue Commissioners v. Blott (1921), 2 A. C. 171.

The language quoted in the appellant's brief from opinions in earlier British cases is utterly in conflict with the later opinions of the higher British tribunals, quoted above. Such statements were not necessary for the decision of the controversies there involved and, as *dicta,* have been entirely discredited by decisions of the House of Lords, the highest court in Great Britain. We do not believe anything would be gained by reviewing them at length.

We submit that the British cases cited above clearly show—

(1) that the income tax of a British company is not paid as agent for its shareholders, but is a tax imposed on and paid by the company, separate and distinct from its shareholders;

(2) that the situation of the company is not affected by the deduction of tax from dividends;

(3) that the relief allowed to shareholders who fall in the exempt class is grounded on the independent consideration that the shareholders ultimately bear the company income tax burden, and that the refunds are made because the company paid income tax—not because the shareholder paid a tax on his dividend; and

(4) that the addition of deducted income tax to the net dividend received by a shareholder, for surtax purposes, is grounded on separate considerations that are not material to the question in issue here.

(d) The Deduction of a Tax From Dividends Under Rule 20 of the British Act Does Not in Any Real Sense Reimburse the Company for Its Own Income Tax Payment.

We have seen that the Crown has only a collateral concern in the deduction of tax from dividends. The question, then, is whether, as between the company and its shareholders, the deduction has the effect of reimbursing the company for a part of its own income tax payment.

The following simple illustration will make it obvious that the company does not gain anything when it deducts tax from dividends. Assume the case of a company that distributes annually all of its profits as dividends. If, in 1921, that company had profits of £10,000; if it paid income tax thereon of £2,000; and distributed £8,000 to its shareholders by means of a declaration of a £10,000 dividend, less tax of £2,000, where is there any reimbursement? The company made £10,000. It paid income

tax thereon to the British Government of £2,000, distributed what remained—£8,000—to its shareholders. The deduction of tax, £2,000, added nothing to the company's wealth.

As between the company and the shareholder, the deduction of tax under Rule 20 merely has the effect of allowing the company income tax as a deduction in ascertaining the amount of profits available for distribution as dividends. As Mr. Justice Rowlatt aptly said in *Purdy v. Rex, supra,*—

> "The company has to pay income tax on its profits as a company, and having paid income tax, the result is there is less to divide among shareholders."

Superficially, it might appear that through deduction of the tax, a British company is allowed to discharge its liability for dividends for less than the declaration obligated it to pay. Upon analysis, it becomes clear that this view is utterly without merit, viz.:

1. Under Rule 20, every British shareholder's right to dividends is subject to a tax deduction. Thus, the shareholder has no right to demand the gross dividend declared by a British company if that company chooses the "less tax" form of declaration. When this form of dividend declaration is adopted, the company's liability to the shareholder is for payment of the "less tax" sum. The practical effect of the Rule is to prevent the shareholders from demanding more than the company can pay without charging its income tax to capital.

2. Nothing is received by the company when it incurs the liability arising from a dividend declaration. Thus, the situation is utterly different from the one where a corporation issues its bonds for cash, and later retires

the bonds at less than the issuing price. There, on the whole transaction, the corporation clearly improves its economic position in the amount of the difference between what it realized for the bonds when they were issued, and the amount it disbursed to rid itself of the liability. In the case of the deduction of tax from dividends, the transaction has no beginning or end. It is all one operation.

3. In the case of dividends, the amount thereof is usually within the reasonably exercised discretion of the management of the company. It would be an odd result if that management were able to fasten a liability on the company by declaring a dividend in excess of what was intended to be actually paid, and then be said to have recouped, or reimbursed itself for a part of that liability through deduction of tax from dividends paid to shareholders.

The truth of the matter is that profits available for dividends, under our conception of law and accounting, have passed tax-paid through the door of income into the capital account of the company. What is done with these profits thereafter in the way of distribution to shareholders is purely a capital transaction and does not give rise *to gain or loss.*

After all, we are dealing here with a United States statute which allows this appellee a deduction from income taxes paid to Great Britain. The purpose of the statute in allowing this deduction was to ascertain net income by deduction from gross income of all proper expenses—foreign taxes being dealt with, as they should be, as an expense item incurred in earning the income subject to our tax. Our statute gives this deduction for foreign taxes "paid". There is no doubt but that the

appellee paid the British taxes in question; and there is no doubt but that it paid them on its own income and for its own account. There is also no doubt but that the taxpayer never received any part of these taxes from its shareholders, in any real sense.

The effect of the appellant's argument is that under British law, the word "paid," as applied to payments of income tax, is construed to mean "paid" and "ultimately borne". In this connection, it is interesting to observe how completely the appellant's conception is at variance with the views of the British courts when they have had occasion to construe the word "paid" as it appears in their own law. The case of the *Commissioners of Inland Revenue v. Dalgety & Co., Ltd.,* 15 T. C. 216, is precisely in point. There the taxpayer realized income in England and also in Australia, all of which was taxable at the British rates. The Australian income had also borne income tax imposed by the Government of Australia. The purely English income was insufficient to meet debenture interest, and the deficiency was met out of Australian income. The question in the case involved the amount of the relief to which the taxpayer was entitled on account of its payment of Australian income tax, under Section 27 of the Finance Act of 1920, which provided as follows:

> "If any person who has paid, by deduction or otherwise, or is liable to pay, United income tax for any year of assessment, on any part of his income, proves * * * that he has paid Dominion income tax for that year in respect of the same part of his income, he shall be entitled to relief from United Kingdom income tax paid or payable by him on that part of his income at a rate thereon to be determined as follows * * *."

It will be noted that the above section has the effect of our own provision allowing a credit for foreign taxes; also, that the British taxpayer seeking relief under the section must prove that he "paid" Dominion income tax on the part of the income on which he "paid" British income tax.

The Crown contended that the relief for Dominion income tax could not be allowed as to that part of the Dominion income that was applied to the payment of the debenture income, for, said the Crown, the burden of tax on that income was borne by the debenture holders from whose interest payments tax was deducted by the company.

The Court of Appeal and the House of Lords held that the relief for Dominion income tax should be given the taxpayer on the ground that the word "paid' 'in the relief section meant exactly what it said, and did not mean, as the Crown contended, "paid and ultimately borne."

Here was an interest case where deduction of tax actually diminished the amount that would otherwise have been payable to the debenture holders,—a much stronger case than where a mere bookkeeping arrangement is made in regard to dividends. Nevertheless, the British court refused to construe the word "paid" as meaning "paid and ultimately borne," as the appellant in our case would have this Court construe the word "paid" as its appears in Section 234 (a) (3), Revenue Acts of 1918 and 1921.

The following is quoted from the opinion of Lord Thankerton in the *Dalgety* case:

> "The Special Commissioners decided in favour of the Respondents, Mr. Justice Rowlatt in favour of the Crown, and the Court of Appeal in favour of the Respondents. I agree with the decision of the

Court of Appeal. In my opinion the natural meaning of the language used is in favour of the Respondent's contention. In accordance with the provisions of the Income Tax Acts the whole of the Company's profits, whether applied in whole or in part in payment of debenture interest, or not so applied at all, forms their income for the purpose of assessment for charge under Schedule D and, in my opinion, the fact that they are entitled, though not bound, to recover the appropriate proportion by deduction on payment of the interest cannot be held to alter the position. The Company are entitled to make that deduction whether they have paid their Income Tax or not; and are under no liability to account to the Crown for it. *The contention of the Crown involves construing 'paid' to mean 'paid and utimately borne', a construction for which I see neither necessity nor warrant.*"

Lord Macmillan, in his opinion, said:

"There can be no question that the Company has paid full United Kingdom Income Tax on the whole of its income, including the portion derived from the Dominions and applied in paying its debenture interest. No deduction from assessment has been made in respect of its debenture interest and none could properly be made. The amount of the debenture interest is not deductible for the purpose of ascertaining the net assessable income of the Company. It is true that the Company will not have borne full United Kingdom Income Tax on the portion of its income derived from the Dominions and applied in paying its debenture interest if the relief claimed is accorded. But the right to deduct Income Tax at the full United Kingdom rate when paying its debenture interest is plainly conferred on the Company

> by Rule 19, for the condition is that the interest shall be 'payable wholly out of profits or gains brought into charge to tax' and the whole profits of the company have been brought into charge to tax. *Actual payment, not ultimate incidence, is the criterion both of the right of relief and of the right to deduct.*"

If under the British law, a company has paid British tax where it has "passed the tax on" to the debenture holders and thereby relieved itself of interest, it certainly has paid British tax where it has declared a dividend either free of tax or less tax, and has merely deducted the so-called tax appropriate thereto.

Whether viewed under the British decisions or under the provisions of our own Act, the appellee paid the tax in question on its own profits and is entitled to a deduction therefor.

(e) Appellant's Construction of the Law Would Result in Administrative Confusion and Serious Danger of Duplicating Deductions.

Appellant apparently takes the position that the correct rule of construction is set forth in S. M. 3040, C. B., IV-1, 198 and S. M. 5363, C. B., V-1, 89, two informal rulings of the Bureau of Internal Revenue. These rulings, promulgated in 1925 and 1926, respectively, hold in effect that the British income tax constitutes a credit or deduction to the stockholder if it is "deducted" from dividends, but that it constitutes a credit or deduction to the corporation if no dividends are paid by the company. We respectfully submit that such a construction, while it might work substantial equity in some cases, lays the emphasis upon the *ultimate burden* of the tax, where the test prescribed by our law is *imposition* and *payment*.

Furthermore, such a construction leads to innumerable administrative difficulties. In the first place it is difficult for our officials to determine what dividends have been paid by a foreign corporation.

Again, it rests the deductibility of the tax upon an event which of necessity is subsequent to the imposition and payment of tax. It would be just as logical to say that the California gasoline tax is deductible by the consumer if he ultimately bears the burden, yet the Department has ruled expressly to the contrary. See G. C. M. 630, C. B., IX-2, 107.

Furthermore, in most cases a corporation declares dividends in a year subsequent to that in which the profits were earned. Years after the corporation has paid the tax and been allowed the deduction, it may pay dividends out of such profits and, under the appellant's construction of the law, the stockholders would be entitled to another deduction. How would our officials be able to protect our tax revenues in such a situation?

Again, under the British law, as shown in the quotations from the opinions of the House of Lords in the *Neumann* case, *supra,* the tax is deducted from the dividend at the rate current in the year of distribution, irrespective of the amount of tax paid by the company. In such a situation, what amount is deductible by the stockholder, the rate of tax actually *paid* by the company or the rate at which the deduction was made from dividends? If it is the amount of deduction, then it may have no relation whatever to the *tax* actually paid to and received by the British government—in other words, it is not a tax deduction. If, on the other hand, it is the rate actually paid by the company, how are our officials to determine out of what profits

in past years the dividend was paid or what rate of tax such profits bore?

The obvious conclusion is that the appellant is attempting to convert a tax actually imposed upon the profits of, and paid by, the company into a tax paid by the stockholder on the basis of subsequent events which may not occur for many years, whereas the theory of our Acts is to treat each taxable year as a unit and ignore events which occur in other periods.

The administrative confusion which would follow from such an interpretation is in itself sufficient rebuttal to appellant's contentions, even if the law were ambiguous. Fortunately, however, the language of our statute is plain. Whether the tax paid by the corporation is deductible depends upon the situation at the time it is paid and cannot be changed retroactively by any subsequent events.

(f) There Has Been no Implied Ratification by Congress of the Interpretation for Which Appellant Contends.

Appellant makes the further contention that reenactment by Congress of the tax deduction and credit provisions in later Acts implies ratification of appellant's interpretation. Such an argument has no foundation.

In the first place, the Departmental rulings referred to above merely set forth an interpretation of *British* law based upon *dicta* in old cases which have been repudiated by the highest courts of England. Furthermore, these rulings were not promulgated until 1925 and 1926, subsequent to the taxable years in question.

The Commissioner has not followed a consistent practice on the question here presented. As a matter of fact, the Bureau is vigorously contending today before the Board of Tax Appeals that stockholders of British corporations are not entitled to a deduction for any "taxes" on dividends paid by such corporations. The Board cases referred to include *George W. Elkins*, Docket No. 75742; *Leslie H. Reed*, Docket No. 75812; *Estate of Marie Cook Hickey*, Docket No. 75849; *Estate of James Hickey*, Docket No. 75852; and *Mary Duke Biddle*, Docket No. 62025. The fact is that the Commissioner is awaiting a final decision by the courts on the question and in the meanwhile is protecting the Government's interests by denying the deduction to both corporations and stockholders.

The only court decision on this question to date is that of the Court below in the present group of cases, and that, of course, was in accordance with appellee's contentions. The case of *Basil Robillard*, 20 B. T. A. 685, cited by appellants, does not represent a considered decision by the Board on this question, for the reason that parties there *stipulated* that the credit should be allowed for amounts deducted from dividends by the British company on account of income taxes, with respect to stock then held by the taxpayer. P. 687, par. 5.) The only question presented to the Board was whether like treatment should be accorded to dividends from a Canadian company which in turn had in turn received dividends from the British Company. The Commissioner having stipulated the propriety of the credit and having introduced no facts or arguments to the contrary, the Board had no alternative but to follow the stipulation.

Obviously, this was not a "decision" at all. On the other point, the Board upheld the Commissioner. Upon appeal by the *taxpayer,* the Circuit Court of Appeals, 2nd Circuit, affirmed without an opinion. On such appeal, the question here involved was not even presented to the Court.

In this connection, attention is invited to *Helvering v. New York Trust Co.*, 292 U. S. 455, where the Supreme Court disposed of a similar contention with the following comments:

> "The Commissioner's suggestion that, by retaining the same definition in the 1924 Act, Congress approved the construction for which he contends is without merit. The definition had not been construed in any Treasury decision, by the Board of Tax Appeals or by any court prior to that enactment * * * The rulings, I. T. 1379, 1660 and 1889, cited by the Commissioner were made before the passage of the 1924 Act but they 'have none of the force or effect of Treasury decisions and do not commit the Department to any interpretation of the law.' See cautionary notice published in the bulletins containing these rulings. It does not appear that the attention of Congress had been called to any such construction. There is no ground on which to infer that by the 1924 Act Congress intended to approve it."

For like reasons, the rulings cited by appellant do not have the force of Treasury decisions and would not be of value even of the statute were ambiguous. However, the language of the law is plain—the word "paid" is hardly susceptible of ambiguity. Under these circum-

stances, "there can be no construction where there is nothing to construe." *United States v. Hartwell,* 6 Wall. 385, 396. See also *Omega Chemical Co.*, 31 B. T. A. No. 200, in which the Board refused to follow what the taxpayer argued was an administrative interpretation of the foreign tax credit provision in the Department's regulations.

We respectfully submit, therefore, that the Court below properly held that appellee was entitled to a deduction for the British income tax imposed on its profits and paid by it.

Conclusion.

For the reasons set forth above, we respectfully urge that no error was committed by the Court below and that the judgment in favor of the appellee should be affirmed.

Respectfully submitted,

JOSEPH D. PEELER,
819 Title Insurance Bldg.,
Los Angeles, Calif.
Counsel for Appellee.

GEORGE M. WOLCOTT,
DONALD V. HUNTER,
922 Southern Bldg.,
Washington, D. C.
Of Counsel.

APPENDIX.

Statutes.

NOTE. The trial court herein agreed to take judicial notice of the British law incorporated in the briefs of counsel [R. 34]. In accordance therewith, appellee is setting forth below all, and only such extracts from the British statutes as were set forth in the briefs in the trial court. In this connection, it will be noted that a number of the provisions of the British statutes which are set forth in Appendix B, attached to appellant's brief herein, were not cited or quoted in the briefs below.

United States:

Section 234 Revenue Act of 1921, provides in part as follows:

> "(a) That in computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions:
>
> * * * * * * * *
>
> "(3) Taxes paid or accrued within the taxable year except (a) income, war-profits, and excess-profits taxes imposed by the authority of the United States, (b) so much of the income, war-profits, and excess-profits taxes imposed by the authority of any foreign country or possession of the United States as is allowed as a credit under section 238."

Identical provisions are contained in section 234 (a) (3) of the Revenue Acts of 1924 and 1926. Similar provisions are contained in section 238 (a), Revenue Act of 1918.

Section 238 (a), Revenue Act of 1921, provides in part as follows:

> "(a) That in the case of a domestic corporation the tax imposed by this title, plus the war-profits and excess-profits taxes, if any, shall be credited with the amount of any income, war-profits, and excess-profits taxes paid during the same taxable year to any foreign country, or to any possession of the United States * * *."

Identical provisions are contained in section 238 (a) of the Revenue Acts of 1924 and 1926. Substantially the same provisions are contained in section 238 (a), Revenue Act of 1928.

Section 234 (b) of the Revenue Act of 1921 provides as follows:

> "(b) In the case of a foreign corporation or of a corporation entitled to the benefits of section 262 the deductions allowed in subdivision (a) shall be allowed only if and to the extent that they are connected with income from sources within the United States; and the proper apportionment and allocation of the deductions with respect to sources within and without the United States shall be determined as provided in section 217 under rules and regulations prescribed by the Commissioner with the approval of the Secretary."

Identical provisions are contained in section 234 (b) of the Revenue Acts of 1924 and 1926. Substantially the same provisions are contained in section 234 (b), Revenue Act of 1918.

Section 327, Revenue Act of 1921, provides as follows:

"Sec. 327. That in the following cases the tax shall be determined as provided in section 328:

"(a) Where the Commissioner is unable to determine the invested capital as provided in section 326;

"(b) In the case of a foreign corporation;

"(c) Where a mixed aggregate of tangible property and intangible property has been paid in for stock or for stock and bonds and the Commissioner is unable satisfactorily to determine the respective values of the several classes of property at the time of payment, or to distinguish the classes of property paid in for stock and for bonds, respectively:

"(d) Where upon application by the corporation the Commissioner finds and so declares of record that the tax if determined without benefit of this section would, owing to abnormal conditions affecting the capital or income of the corporation, work upon the corporation an exceptional hardship evidenced by gross disproportion between the tax computed without benefit of this section and the tax computed by reference to the representative corporations specified in section 328. This subdivision shall not apply to any case (1) in which the tax (computed without benefit of this section) is high merely because the corporation earned within the taxable year a high rate of profit upon a normal invested capital nor (2) in which 50 per centum or more of the gross income of the corporation for the taxable year (computed under section 233 of Title II) consists of gains, profits, commissions, or other income, derived on a cost-plus basis from a Government contract or contracts made between April 6, 1917, and November 11, 1918, both dates inclusive."

Identical provisions are contained in section 327, Revenue Act of 1918.

Section 328, Revenue Act of 1921, provides as follows:

> "Sec. 328 (a). In the cases specified in section 327 the tax shall be the amount which bears the same ratio to the net income of the taxpayer (in excess of the specific exemption of $3,000) for the taxable year, as the average tax of representative corporations engaged in a like or similar trade or business bears to their average net income (in excess of the specific exemption of $3,000) for such year. In the case of a foreign corporation the tax shall be computed without deducting the specific exemption of $3,000 either for the taxpayer or the representative corporations.
>
> "In computing the tax under this section the Commissioner shall compare the taxpayer only with representative corporations whose invested capital can be satisfactorily determined under section 326 and which are, as nearly as may be, similarly circumstances with respect to gross income, net income, profits per unit of business transacted and capital employed, the amount and rate of war profits or excess profits, and all other relevant facts and circumstances.
>
> "(b) For the purposes of subdivision (a) the ratios between the average tax and the average net income of representative corporations shall be determined by the Commissioner in accordance with regulations prescribed by him with the approval of the Secretary.

"In cases in which the tax is to be computed under this section, if the tax as computed without the benefit of this section is less than 50 per centum of the net income of the taxpayer, the installments shall in the first instance be computed upon the basis of such tax; but if the tax so computed is 50 per centum or more of the net income, the installments shall in the first instance be computed upon the basis of a tax equal to 50 per centum of the net income. In any case, the actual ratio when ascertained shall be used in determining the correct amount of the tax. If the correct amount of the tax when determined exceeds 50 per centum of the net income, any excess of the correct installments over the amounts actually paid shall on notice and demand be paid together with interest at the rate of 1/2 or 1 per centum per month on such excess from the time the installment was due.

"(c) The Commissioner shall keep a record of all cases in which the tax is determined in the manner prescribed in subdivision (a), containing the name and address of each taxpayer, the business in which engaged, the amount of invested capital and net income shown by the return, and the amount of invested capital as determined under such subdivision. The Commissioner shall furnish a copy of such record and other detailed information with respect to such cases when required by resolution of either House of Congress, without regard to the restrictions contained in section 257."

Identical provisions are contained in Section 328, Revenue Act of 1918.

Great Britain:

(1) Cited in appellee's briefs below.

The income tax provisions of Great Britain for the years in question, as set forth in "The Income Tax Act 1918 and Finance Acts 1919 to 1925 inclusive" as published by His Majesty's Stationery office shows that the tax is levied and collected under five schedules as follows:

SCHEDULE A—On property in lands and buildings

SCHEDULE B—On occupation of lands and buildings

SCHEDULE C—On income from Government securities

SCHEDULE D—On annual gains, profits, etc.

SCHEDULE E—On income from Government securities

Appellee was assessed under Schedule D and the provisions relating thereto are as follows:

Schedule D, paragraph 359:

"1. Tax under this Schedule shall be charged in respect of—

"(a) The annual profits or gains arising or accruing—

"(i) to any person residing in the United Kingdom from any kind of property whatever, whether situate in the United Kingdom or elsewhere; and

"(ii) to any person residing in the United Kingdom from any trade, profession, employment, or vocation, whether the same be respectively carried on in the United Kingdom or elsewhere; * * *.

"2. Tax under this schedule shall be charged under the following cases respectively; that is to say,—

* * * * * * * *

Case VI.—Tax in respect of any annual profits or gains not falling under any of the foregoing cases, and not charged by virtue of any other Schedule;

and subject to and in accordance with the rules applicable to the said cases respectively."

Under the heading "Miscellaneous Rules Applicable to Schedule D," the following is provided at paragraph 394:

"1. Tax under this schedule shall be charged on and paid by the persons or bodies of persons receiving or entitled to the income in respect of which tax under this schedule is hereinbefore directed to be charged."

Section 237, Act of 1918, provides in part as follows:

"In this Act, unless the context otherwise requires:

* * * * * * * *

" 'Body of persons' means any body politic, corporate, or collegiate, and any company, fraternity, fellowship and society of persons, whether corporate or not corporate."

Under the heading "General Rules Applicable to Schedules A, B, C, D and E" at paragraph 420, there is the following provision:

"1. Every body of persons shall be chargeable to tax in like manner as any person is chargeable under the provisions of this Act."

Under the same heading at paragraph 439, there is the following provision:

> "20. The profits or gains to be charged on any body of persons shall be computed in accordance with the provisions of this Act on the full amount of the same before any dividend thereof is made in respect of any share, right or title thereto, and the body of persons paying such dividend shall be entitled to deduct the tax appropriate thereto."

An identical provision was contained in section 54, Act of 1842, referred to in some of the British cases cited below herein.

(2) *Additional provision cited in appellant's brief below.*

> "444 (Section 23, Act of 1918) (1). A person who refuses to allow a deduction of tax authorized by the Act to be made out of any payment, shall forfeit the sum of fifty pounds.
>
> "(2) Every agreement for payment of interest, rent, or other annual payment in full without allowing any such deduction shall be void."